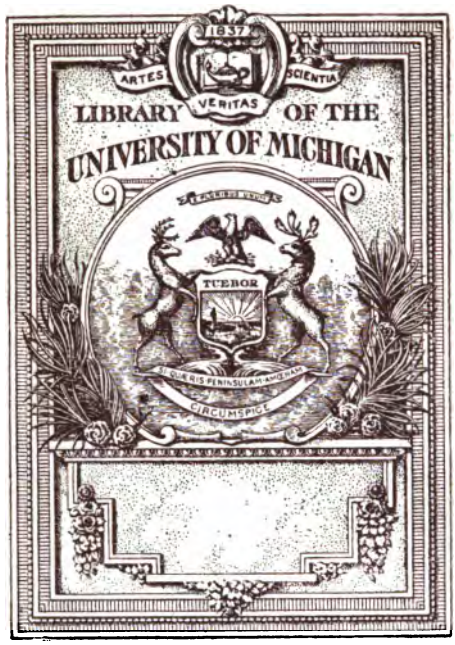

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The State Tax System
of
Washington

by

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Preface

The question of taxes is one in which a large number of persons have a direct personal interest. That present arrangements are unsatisfactory is the opinion of more than one overburdened taxpayer. "Unsatisfactory" is far too mild a term to express the views of tax experts in regard to such a system as that now in use. A change of some sort is sure to come, and it is of great importance that the voters should know along what lines this change should be made.

It is to show in a clear, concrete way what the present system is and why a change is needed, and to suggest some possibilities for improvement, that this book was written. In order that the present system and suggestions for reform, made here or elsewhere, may be fairly criticised a chapter on fundamental principles of taxation is included. For those who wish a good brief book on the general subject of taxation Professor Plehn's "Introduction to Public Finance" is recommended. Professor Seligman's works, especially his "Essays in Taxation," contain careful and very thorough studies of many important points. For discussions of the practical problems with which American states are confronted the proceedings of the annual conferences on the subject, published by the National Tax Association, should be consulted.

While assuming full responsibility for the work, the author wishes to acknowledge special indebtedness to the State Board of Tax Commissioners, particularly to Mr. J. W. Brislawn; to Mr. A. E. Parish, who at the time the chapters on county assessment were written was Assessor of King County; and to Dean J. Allen Smith, of the University of Washington.

VANDERVEER CUSTIS.

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Chapter I.

INTRODUCTION

§1. Justly proud though the citizen of Washington may be of his State, he realizes, if he happens to hold much property, that the burden of public expenditures is rather heavy. Once every two years legislators are sent to Olympia. They promise economy; but if taxes are not increased as a result of the session the taxpayers are inclined to regard themselves as fortunate.

When any reform of the tax system is proposed, the criticism is likely to be offered that the real difficulty is in the amount of expenditures. If these be increased, larger revenues are needed; and, this means increased taxes. While it must be admitted that there is a considerable amount of public extravagance, and that economy and efficiency in expenditure are greatly to be desired, it should be realized that the increase in expenditures is almost certain to continue. With the growth of population and the increasing complexity of civilization it costs more for the State to perform its old functions and new functions are frequently added. Even when allowance is made for the increase in wealth it is by no means improbable that in the future a larger proportion of the income of the people will be spent by the public authorities than has been the case in the past. Against this, of course, must be set the greatly increased benefits that will be conferred by the State.

It does not seem to be generally appreciated that while the amount of taxation will continue to be large the burden would be easier to bear if it were more equitably distributed. This does not necessarily mean that methods should be devised for placing a larger share of the burden on the great corporations or on those who happen to have more wealth than the average citizen. While it is doubtless true that some corporations are escaping their fair share, there is reason to believe that others are unduly taxed. While some persons of moderate means are contributing heavily there are others, equally able to pay, who are contributing little. The question is not one of how the burden can be placed on the few to the relief of the many, but of how it can be justly distributed among all classes.

A bad system of taxation not only works injustice between different members of society; but it may hamper business, discourage the

accumulation of capital, on which the welfare of nearly all classes is largely dependent, and so check the development of the community as to place it at a disadvantage in the great evolutionary struggle in which nations, states, and municipalities, as well as individuals, are engaged.

An unjust system of taxation may actually encourage public extravagance. It is almost certain to do so if it places the burden chiefly on the few when political power is in the hands of the many. If, while actually distributing the burden widely, it appears to place it on the few similar results are likely to follow, since, as an influence determining political policy, what is is often of less importance than what is believed to be. The system existing in this State probably does result in a wider distribution than is generally realized; and in this condition is doubtless to be found one of the causes of the present extravagance.

§2. In devoting attention to taxation rather than to expenditure it is not the intention of the author to minimize the importance of public economy. That is a separate problem, and it is one well worthy of study. Admitting this, the author feels that, under existing conditions, a consideration of the tax system will prove to be even better worth while. Since, however, the need of economy in expenditure is so strongly felt, it will be well to say a few words in regard to it at this point.

Unfortunately the conditions under which appropriations are made, in this as in most other states, are very unfavorable to an intelligent and economical financial policy; and a reform of budgetary procedure is one of the first steps that should be taken for the prevention of unwise expenditure.[1] For a satisfactory system two things are essential: a definite location of responsibility; and a well considered financial program. Until recently we have had neither. The Legislature, at its last session, made provision for a new system. Hereafter state departments, commissions, institutions, and offices are to report to the State Board of Finance, not later than October 15th of each even numbered year, an itemized estimate of their expenses for the coming biennium. The State Auditor is to assemble these estimates, showing existing appropriations and the amounts expended up to September 30th. He is also to set forth the revenues

[1]For a discussion of this subject, with definite suggestions, see L. M. Livengood, "A Budget System for the State of Washington," in "Taxation in Washington," Bulletin of the University of Washington, University Extension Series, No. 12. This bulletin will hereafter be referred to simply as "Taxation in Washington."

of the State up to that date and the estimated receipts for the coming biennium. The needs of the departments, etc., as set forth in their estimates, are to be examined by the State Board of Finance, which may demand additional information, and may make its own inspections, examine books, and administer oaths. On the basis of the information thus acquired it is to make its recommendations to the Legislature.

The new law seems to provide for the preparation of a financial program; and if the work is well done a distinct step in advance will have been made. How great a step it will be is something that only the future can disclose. In any event it is only a step. A financial program, which may be well considered, must be submitted to the Legislature; but what the Legislature will do with it remains to be seen. Centralization of responsibility still seems to be lacking. Any member of either house may submit a bill relating to revenue or expenditure; and at every session a number of bills are introduced, some of which are of value chiefly in the gaining of political support for the member introducing them. Bills are commonly referred to a committee; but there is no one committee which can be held responsible to the people as a whole or whose action is definitely that of the administration. Fortunately the Governor has the right to veto particular items in a bill; but except in cases which he regards as particularly bad he is naturally inclined to shift responsibility to the Legislature. The right of referendum is retained by the people, but it does not apply to legislation necessary for the immediate preservation of the public peace, health, or safety, or the support of the state government and its existing institutions. In any event the referendum is slow in action, and is unsuitable for dealing with matters of this sort.

Budgetary procedure is more highly developed in local than in state finance. County commissioners, city and town councils, and directors of school districts lying in whole or in part within the limits of incorporated cities or towns are required to make annually itemized lists of estimated expenditures, together with estimated receipts from other sources than taxation, and a statement of the amounts which it is proposed to levy. Notice must be given of the time and place of a meeting at which taxpayers may appear and be heard for or against the proposed levies. After this taxes are voted in specific sums which must not exceed the amounts named in the estimates. A law imposing such requirements as these does not, of course, guarantee the use of

a well considered budget; but it at least goes a long way towards providing the necessary machinery.

§3. It is only with that part of the budget that deals with revenue that we are now concerned, and even here only with the items that have to do with taxation. In order, however, to make clear the nature of the taxation and its place in the revenue system we shall here pause, for a moment, to consider very briefly the different sources from which the State derives its income.

As the term is here used, "a tax is a compulsory contribution of the wealth of a person or body of persons for the service of the public powers,"[2] levied without regard to any particular service to, or on account of, the contributor. Strictly, the word wealth should be held to include services. Of these the most important in this country, at least in times of peace, is jury duty. In our consideration of the tax system, however, we shall omit all reference to contributions of services, confining our attention to those forms of taxation that are paid into the public treasury.

A fee differs from a tax in that it is imposed to defray, in whole or in part, the expense involved in some governmental action which is occasioned by the person from whom the payment is required or confers upon him a special benefit. As examples of fees may be cited the payments required for inspection of various kinds, for the issuance of certificates, and for some of the services rendered by the courts. In definitions of the fee the idea is commonly expressed that it is a payment for a special benefit. As regards some kinds of fees this is legitimate enough; but there are others of such a character as to make it necessary to point out that the special benefit may be such "by legal fiction" or "arbitrarily so considered." In any event the payment should not exceed the expense involved. If it does it should be regarded as part fee and part tax.

Prices, in this connection, are payments to the government that rest primarily on a commercial basis. They include rentals and interest as well as payments for the purchase of goods or services. Prices are more conspicuous in municipal than in State finance. Cities often sell water, gas, and electricity. The State, however, is not without revenues of a commercial character. Washington owns a considerable amount of real estate from which it receives rentals. Funds are invested in securities from which interest is received. Money on hand is deposited at interest in the banks. In these cases

[2]Bastable, "Public Finance" (third edition), p. 263.

the State, though possessed of sovereign power, puts itself in substantially the same position as would be occupied by a private individual or a corporation rendering the same service. Where, however, the government exercises monopoly powers and charges a price that, as a price, is unduly high the element of taxation is present.

To examine all the fees and prices charged by the State in order to determine whether or not they contain an element of taxation would be a long and difficult task, and for present purposes it would hardly be justified. We shall therefore treat as taxes those that are primarily such, and shall leave out of account other forms of payment that contain a small element of taxation. There are some "fees," however, which yield so much revenue above the expenses of the services in connection with which they are made as to require consideration.

Besides the three forms of income just mentioned the State derives a certain amount of revenue, probably larger than is generally realized, from escheats or the reversion of property for which no lawful owner can be found, from gifts, and from penalties. The mention of gifts may seem strange, yet Washington, like many of the other states, has received large grants of land from the nation, and even now receives annual gifts or subventions for specified purposes, such as the maintenance of certain forms of education and the Soldiers' Home. Gifts from private individuals are, perhaps, less common in the case of state than in that of municipal finance, yet considerable gifts are sometimes made to state institutions. One example is the Gatzert Foundation of Child Welfare at the State University.

A considerable amount of money is sometimes secured through public borrowing, through the sale or redemption of securities held for investment, or through the sale of other property. Receipts of this class may be of great importance; but, except so far as a profit is made from such transactions they belong to the capital rather than to the income account.

While there are a few cases in which classification is difficult, taxes are generally so different in nature from other forms of revenue as to make a separate consideration of the tax system practicable. Its compulsory character makes it important that consideration be given to its efficiency. The weight of the burden renders especially significant the problem of its just distribution. The fact that the revenues are used for general purposes raises the questions of what justice in taxation is and how it can be secured.

§4. In our study of existing conditions we shall confine our attention almost exclusively to the state system. Local taxation is, of course, heavier, and from that point of view is of more importance. As a matter of fact, however, a study of the state system will nearly cover that of the localities. Most of the local tax revenues are drawn from the same system as those of the State. The chief differences are to be found in the amount of the taxes levied, and consequently in the rates that are imposed. Indeed, from one point of view, it might be said that we are really studying the local system with special reference to the State. The general property tax is by far the most important and this is administered chiefly by officials elected by the counties, though subject to state supervision. Liquor licenses—now things of the past—were, most of them, locally administered; but the State got its share and attention will be given them in that connection. The other taxes collected by the political subdivisions of the State are of much less importance.

For the purpose of our study, the system of the State may be divided into three main groups: the general property tax; taxes on corporations and business; and the inheritance tax. The first of these is really a very complex system in itself, and from several points of view, including that of revenue, is of more importance than all the rest combined. Taxes on corporations and business include various license, franchise, and privilege taxes, as well as some fees that are so large as to include a considerable measure of taxation. In this connection we shall consider one or two kinds of payments which while not strictly business taxes bear some resemblance to them. The inheritance tax is one definite tax, and while not without some defects, is one of the best taxes we have.

Chapter II.

SOME FUNDAMENTAL PRINCIPLES

§1. One of the first points to be considered in the study of any existing institution is its purpose. To any question on this score as regards taxation the answer may appear obvious: its purpose is to raise revenue. This, indeed, is implied by our definition of taxation. In practice, however, what are commonly called taxes are not infrequently levied for other purposes, such as the regulation of industry or a modification of the distribution of wealth. In some instances revenue is hardly a consideration at all. Such is the case with the federal "tax" of ten per cent on the notes of state banks. The state "tax" of $300, levied in connection with the Red Light Abatement Act, is really a penalty rather than a tax. In some instances revenue is an important but perhaps a secondary consideration. Such is the case with the protective tariff and the license taxes imposed on certain kinds of business, such as that of dealing in alcoholic liquors. Numerous plans have been suggested for taxes designed to cure the "unjust distribution of wealth" and, incidentally at least, to secure a revenue, such as the tax on "swollen fortunes" or a very heavy tax on large incomes.

"Taxes" that in purpose and effect yield no revenue or only an insignificant amount need hardly be considered in a work on taxation. From an economic point of view they are not taxes at all. They are more like fines; and the fact that they have the form of taxes is often due to constitutional difficulties in the way of dealing with the matter more directly.

When a tax is used for two different purposes, such as the raising of revenue and the regulation of industry, two distinct things are confused, and the result is likely to be that one or both purposes is badly served. If the tax be not entirely unsuited to at least one of them the rates and methods of levy appropriate for the two are very likely to be different. Where, for example, one object is to restrict a business the tax, generally speaking, will yield a revenue only so far as it fails to restrict, and will restrict only so far as it fails to yield a revenue. In practice the result is often a compromise that is satisfactory from neither point of view. The objection to the use of a tax for a double purpose, however, is only a *prima facie* one. It may be overcome by special considerations.

While we are not here concerned with federal finance, the protective tariff furnishes an excellent example. If the tariff be sufficiently high to give the market to domestic producers it yields no revenue: in so far as it is low enough to permit foreign goods to enter the country it fails to protect home industry. Nor is this all. The experience of the United States has been that while a large revenue has been secured it has been unstable in amount and very difficult to control. More than once, in times of need, especially in time of war, the revenue has been insufficient, and at other times a large surplus has led to extravagance.[1] These difficulties are not entirely due to the protective feature, but there can be little doubt that they have been greatly aggravated thereby. Moreover, the protective feature makes adjustment for financial reasons difficult; and financial considerations stand in the way of reform from the point of view of protection. Revenue is certainly desirable, and protection may be, but the combination of the two, even if justified, has some very unfortunate features.

Another illustration is furnished by liquor licenses. If it be decided that the liquor business should be conducted by private individuals for profit, subject to restraint and regulation, there is something to be said in favor of a high license policy. Such taxes yield a large revenue and are easily collected. They restrict the business, and tend to concentrate it in a relatively small number of establishments, thus making supervision easier. In some cases the fact that a high tax must be paid for a license makes the latter so valuable that the liquor dealer will take care that he does not lose it through a violation of the law. This, however, is about all that can be said in favor of high license as a means of regulation; and it must be admitted that the liquor problem remains unsolved. It may at least be seriously questioned whether the desire for revenue has not in some cases led to a faulty administration of the liquor laws. Regulation by high license rests, moreover, on an assumption as to the sort of regulation needed. On almost any other assumption the large revenue derived from the business is a serious obstacle in the way of dealing with the problem on its merits. In more than one case the fear of losing revenue has furnished a strong argument against the elimination of the saloon.

[1]See Hoxie, "The Adequacy of the Customs Revenue," Journal of Political Economy," Vol. III., pp. 43-64; reprinted under the title "The Customs Revenue of the United States," in Bullock's "Selected Readings in Public Finance," Ch. XVIII.

The propriety of taxation as a means of regulating the distribution of wealth is even more doubtful. Indeed, in all the proposed forms with which the author is familiar it would be dangerous. In so far as great fortunes are the result of payment for services rendered, taxation, if successful in its object, would in all probability lead men either to render less service or to spend their incomes in extravagance. In either case the accumulation of capital would be checked; and capital is one of the factors in the productivity of industry, on which the prosperity of nearly all classes, not in the least excepting labor, is dependent.

The present gross inequality in the distribution of wealth is due to underlying causes. Unless there is an almost incredible inequality in individual capacity these causes must be found in the economic conditions. Merely to tax the rich for the benefit of the poor is to treat the symptoms, not the disease; to hit at results, not at causes. So far as it gives relief it is very like an opiate, deadening pain, indeed, but lowering vitality, killing ambition, drawing attention away from the real causes of the evil, and allowing them to grow in strength. There is, of course, a legitimate field for the use of opiates, and the same may be said of taxation as a means of dealing with the unequal distribution of wealth. It must not, however, be supposed for a moment that it is a remedy or that it can be used without danger. To apply a real remedy will doubtless cost money that must be raised by taxation; but such taxation will be laid on different principles than those taxes designed to alter directly the distribution of wealth.

§2. The expenditures of the state are justified by the benefits resulting; and in so far as the purpose of taxation is to provide the necessary revenues it follows that the justification for taxation is to be found in the benefits conferred by the state. It must not be inferred, however, that the amount of taxes that each should pay depends on the benefit that he individually receives. The state is no mere cooperative association, formed to confer benefits on particular individuals at a price. Such functions it may have; but above and beyond these, it is an organization formed for the maintenance of conditions on which the life and prosperity of its members depend. No one who admits that the state may, if necessary, rightfully demand of individuals the sacrifice of life or health on the field of battle can logically hold that its rightful claim is limited to payment for benefits received. To those who deny the premise it need only be

said that the laws of natural selection will take care of a state built on such a denial; and the place thereof will know it no more.

Where the state confers what are distinctively individual benefits a payment upon that basis may legitimately be collected. Such payments, however, are in the nature of prices or fees. Taxation is imposed for defraying the expenses due to general functions, such as the securing of the rights to life, liberty, and the pursuit of happiness. To take but one example, the support of an educational system by taxation is justified, not so much by the benefit conferred on the individuals directly affected, as by the fact that a state in which an educational system, open to all, is maintained is stronger, better, and happier than one in which it is not. The State of Washington is justified in spending millions of dollars on its University, not primarily because of the benefit derived by a few thousand students, constituting but a small percentage of the population, but because by reason of the University the State—that is, the people taken as a whole—is better fitted to survive in the evolutionary struggle and to prosper. In so far as the University is successful those who benefit most directly are assets to the State or at least to mankind, of which the people of the State are a part; and the same may be said of the results of research.

Where the benefits are common, taxation according to benefit is impossible, partly because the individual's share is impossible to estimate. It is true that in most cases some benefit may be directly attributed; but if we were to attempt to apportion taxation on this basis, ignoring all benefits that cannot be directly traced, the results would be startling. One of the chief functions of the State is to protect life and liberty. Unless we are to assume that the rich man benefits more largely by life and liberty than does the poor man, taxes for the performance of this function should be distributed equally; and a heavy poll tax would be in order. Taxes for the protection of property might, indeed, be larger in the case of the rich man than in that of the poor man, but it is not certain that they would be larger in proportion to the amount of property held. As regards expenditures for education it would seem that, ignoring all public benefit, the poor man benefits more largely than does the rich, partly because the poor man, generally speaking, has more children, and partly because the rich man is better able to provide for his own. The rich bachelor would, of course, escape taxation on this account entirely. From these examples alone it will be seen that taxation according to the benefit

that can be traced is impracticable. Not only would it violate our sense of justice; but it would make impossible many expenditures necessary to build up a great and prosperous commonwealth.

Upon the whole the most satisfactory basis for taxation seems to be ability. If each contributes to the common expenses according to his ability it would seem that the sacrifice or hardship resulting from the burden would be as small as possible, and that many very desirable expenditures could be made which, under any other system, would be impracticable. Considering the nature of the expenses defrayed by taxation, apportionment according to ability seems to be consonant with justice. Where the benefits of a given line of expenditure accrue chiefly to a given community or class special taxes may be imposed; but within that community or class they should be apportioned on the basis of ability.

To taxes laid on this basis the objection is sometimes raised that they place a penalty on success. Now, it may be admitted that taxes may be laid in such a way as to discourage thrift, energy, and enterprise. If, however, they are actually laid according to ability they do not really fall more heavily upon the successful man than upon the unsuccessful. The former, indeed, pays a larger amount but the burden is no greater than in the case of the latter. Moreover, aside from the question of justice, the taxation of inability and failure would hardly be satisfactory from a revenue point of view. To be sure, it is not desirable to tax thrift and exempt extravagance; but neither is this taxation according to ability. In some cases men come into possession of wealth that they have not earned. In so far as this is done illegitimately taxation is hardly a proper method of dealing with the situation. So far as such wealth is legitimately acquired it may be regarded as conferring a special measure of ability. Cases of this sort, however, at least in the opinion of the author, are much less important than is sometimes supposed.

§8. More than a century ago Adam Smith set forth four canons of taxation which have since become famous. These are equality, certainty, convenience, and economy.[2]

Smith defined equality in taxation as taxation according to ability, "that is" in proportion to the revenue enjoyed under the protection of the state. With the view that taxation should be according to ability we can heartily agree, but that this can be attained by taxation in proportion to income is at least open to question. An income

[2] "Wealth of Nations," Bk. V., Ch. II., Pt. II.

of $500 a year is insufficient to decently maintain a normal family, and it would seem that a man with an income of $5,000 would be in a much better position to pay $50 than a man with $500 would be to pay $5. Upon the whole it would seem that ability increases more rapidly than income, and that taxation should be "progressive"; that is, the rate should increase with the increase in income. Just how much more rapidly it should increase is a difficult question; and it must be admitted that we have not sufficient data to make possible a satisfactory answer. Nor, as we shall see in a few moments, is this the only difficulty with income as a measure of ability.

It should be noticed that the canon of equality applies to the tax system as a whole, rather than to any particular tax. It is a small matter if one tax falls more heavily on one set of people and another on another, provided that the final result is that each pays taxes according to his ability.

The other three canons, while important, are so obvious that they can be dismissed with brief comment. They apply, not merely to the tax system as a whole, but to each tax. By certainty is meant that the tax that each is called upon to pay should not be arbitrary or left to the discretion of officials. The taxpayer should know just how much he has to pay, when, where, and to whom. So important did Smith regard this canon that he held a considerable degree of inequality to be a much smaller evil than a small degree of uncertainty. The canon of convenience states that the conditions of payment should be made as convenient as possible to the taxpayer. Finally, the canon of economy requires that the tax should take out and keep out of the pockets of the people as little as possible over and above what it puts into the treasury. This means that it should be inexpensive to collect and should not unnecessarily obstruct industry, offer the temptation to risk the penalties of evasion, or subject the taxpayer to annoying inquisition.

§4. A very important distinction is that between direct and indirect taxation. Unfortunately there is no single clear-cut definition of either of these terms. Among all disagreements, however, two ideas stand out with special prominence. The first of these may be called the economic and the second the administrative point of view. According to the economic definition, a direct tax is one the burden of which rests upon the person from whom it is collected. Generally speaking, this is true of an income tax. An indirect tax is one the burden of which is shifted from the person who pays it in the first

instance to someone else. A customs duty, for example, is collected from the importer, but usually it is shifted, in the form of increased prices, to the ultimate consumer. From the administrative point of view a direct tax is one that can be calculated in advance and lists of taxpayers prepared. This is true of the general property tax. An indirect tax is one that is laid upon some circumstance, act, or event, such as the number of gallons of whisky distilled. The two ideas are, perhaps, best brought out when it is said that the economic definition turns on the incidence of taxation, the administrative on the possibility of using tax rolls.

In considering equality in taxation the economic point of view is the more important. The study of the incidence of taxation is an exceedingly difficult one, but it is possible to lay down a few general principles. Ordinarily a tax can be shifted only if the person from whom it is collected can raise the price at which he sells goods or services, or lower the price at which he buys them. Since price depends on demand and supply it is only when the conditions of demand or supply are affected that the tax can be shifted. Even then the shifting may take place slowly, so that the incidence of an old tax may be different from that of a new one similar in character.

Suppose, for example, that a tax of a given per cent is laid on the rental value of all land, and collected from the owner. Obviously the demand for land is not affected. Neither is supply. Clearly the quantity of land remains the same. The owners would gain nothing by taking it off the market. To be sure the rent left to the owner is reduced by the amount of the tax, but if he withholds the land from use he will get no rent at all, and meanwhile he will have to pay the tax. If he tries to sell the land the price he can get for it will be lower by reason of the tax. The tax will therefore rest upon the owner. It will not be shifted.

Suppose now a tax is laid on the rental value of houses, but not on that of other forms of capital. The building of houses becomes less profitable. Fewer houses will therefore be built, and if demand is not increasing, some of the old ones, as they become unfit for use, will not be replaced. In either case the supply, at the old price, will not be equal to the demand. The rent that will be paid for the use of a house will therefore rise and the tax will be shifted, at least in part on the tenant.

Much, however, depends on the universality of the tax. If it were laid on every possible line of investment in proportion to the

ability that each represents and successfully administered, there would be no investment to which capital could turn to escape the tax. Only so far as the result was a reduction of saving, and therefore a reduction in the supply of capital would the tax be shifted. If the tax were reasonable in amount the effect would probably be slight and the tax would be shifted only in a small degree if at all.

An excellent illustration is furnished by the attempt to tax investment securities. Mortgages are matters of record and they can therefore be found by the assessors. Stocks and bonds are very difficult—in many cases practically impossible—to reach. In any event capital can leave the taxing jurisdiction. The result has been that men with money have preferred to invest it in forms that escape taxation. Interest on mortgages has risen, not merely by the amount of the tax, but by an additional amount to cover the cost of shifting.

§5. Indirect taxes have some great advantages. They are generally convenient and are commonly easy to administer. The very fact that they can be shifted reduces the temptation to evasion. They can be made to yield a large revenue as is shown by the taxes imposed by the United States, most of which are indirect. The shifting of taxation tends to remedy certain inequalities since if any line of business is unduly taxed it is very likely that prices will rise and the tax be shifted to the consumer.

Right here arises a serious difficulty: the ultimate incidence of the tax may be very unjust. Taxes on commodities, for example, if they are to raise a large revenue, must ordinarily be laid on articles of wide consumption. For these the poor pay a larger percentage of their income than do the rich, and the tax therefore falls more heavily on them. There are some articles of luxury from the taxation of which a considerable amount of revenue can be raised, but, upon the whole, taxes on luxuries are less likely to be highly productive than taxes on the ordinary comforts and necessities of the people. Not only are the total sales of the former likely to be relatively small, but the tax, if heavy, may result in a considerable reduction in the number of sales.

It is possible that a system of indirect taxes might be devised that would be fairly equal in its operation. Where the shifting of the tax can be followed and the incidence determined with a reasonable degree of accuracy the inequality may be a small matter, since taxes that, considered by themselves, err in one direction may be offset by taxes that, considered by themselves, err in the other di-

rection. In general, indirect taxes are likely to fall with undue weight on the poor or moderately well to do; but direct taxes may be made to fall chiefly on the rich. One of the chief reasons for the federal income tax, with its very high exemption and its progressive rates, was the desire to offset the regressive character of the other federal taxes. It can, however, hardly be regarded as more than a step in the right direction.

Even when the difficulty due to the natural inequality of indirect taxes is satisfactorily dealt with, other difficulties remain. One of the most serious of these is the fact that the burden of indirect taxes is not fully realized by the ordinary taxpayer. It may appear to some that this is not wholly an evil. If a man does not know that he is being taxed, it may be said, he does not feel the burden. The trouble is that he does feel it, although he does not recognize its character. It is apt to show itself in the "high cost of living," and this he feels keenly enough. It may be possible to demonstrate to him the fact that taxation is an element in the high cost of living; but it is more difficult to make him realize it; and consequently he is less likely to appreciate the importance of economy in public affairs. One of the great faults of indirect taxation is that it conceals the facts.

Now, if, in a community in which practically every citizen who has attained his majority has the right to vote, it be held that the people, when they realize the burden, cannot be trusted to approve expenditures necessary for the public welfare; or if it be held that they will provide tax laws that are grossly unjust; there is much to be said in favor of relying mainly on indirect taxation. If, however, these premises are rejected it seems highly desirable, not only that every citizen should pay taxes according to his ability, but that he should know that he pays. That such a condition should exist, at least in a large measure, seems to be essential if democratic government is to be regarded as a success. As a practical proposition this implies that every citizen should pay a direct tax, varying in amount with the public expenditures.

It may frankly be admitted that the ideal can hardly be fully attained, at any rate under existing circumstances. Even if it were not true that taxes intended to be direct are in fact often shifted, it would be difficult to devise appropriate direct taxes, especially where there is as much poverty as exists today. In many cases the amount of the tax would be so small that it would hardly be worth the cost of collecting it. Nevertheless, in any consideration of the reform of

the tax system the ideal should be kept in mind, and as nearly as possible realized.

§6. Two important and more or less closely related characteristics of a good tax are stability and elasticity. In so far as the needs of the government are constant, or are changing in a regular manner it should be unnecessary to make changes in the form or rate of the tax. Taxes that vary greatly with every change in conditions are seriously defective. Moreover, the taxing authority should know, at the time provision is made for the tax, at least approximately how much it will yield. Otherwise the treasury is practically certain to be confronted with a surplus or a deficit. Our experience has been that the former is a strong temptation to extravagance. On the other hand a deficit is likely to be expensive since it ordinarily implies public borrowing in some form or other. Under conditions that make borrowing difficult it might well prove dangerous. In the second place, some variation is necessary, for the amount of public expenditures cannot be kept constant. There should therefore be at least one tax in the system that can readily be adjusted to meet the needs of the state. Stability and elasticity are not necessarily contradictory virtues. Where the first is present the revenue will not vary greatly, though it may grow with the development of the community, unless a change is made in the form or rate. Where the second virtue is present a change in the form or rate can be made, if necessary, with some confidence as to the result.

Stability can best be attained by imposing the tax on some stable base, that is on a subject that remains fairly constant, or, better, grows with the development of the community but does not vary with short time fluctuations. In this respect property is a better base than income, although from some points of view income taxes are to be preferred to property taxes. Stability in taxation implies, of course, that the burden will be heavier in times of depression than in times of prosperity. This is an evil, but it cannot well be avoided under any system. It is practicable only to a very limited extent to adjust expenditure to income.

It may be said that this is what the individual or the private business must do; but there is a very important difference. The invidual who spends his entire income as fast as he receives it is either pursuing a very unwise policy or is acting under the pressure of a very unfortunate necessity. In either case the result is likely to be disaster. A successful business is ordinarily run at a profit that

can be temporarily reduced without bringing ruin; and, even so, it is bad business policy to divide the entire profit each year, leaving nothing for emergencies. The state, however, endeavors, as a rule, to collect each year by taxation only the amount needed for current expenditures. Modern governments are not well adapted to the handling of reserves. The duty of carrying reserves is left to the people. The individual should regard taxes as one of his most necessary expenses, and it is not primarily upon these that the results of a temporary reduction of income falls.

One method of adjusting public revenue to expenditure is by the apportionment of the tax. By this is meant that the taxing authority does not directly fix the rate at which the tax shall be imposed, but determines instead the amount of money to be raised, leaving to administrative officials the calculation of the necessary rate. This, of course, brings about a fairly accurate adjustment, and if the subjects of taxation are well chosen does not necessarily mean violent fluctuations, although uncertainty here is substituted for uncertainty in the amount of revenue. As has already been pointed out, however, the need for elasticity makes it important that there be at least one tax the rate of which can be changed frequently without excessive hardship or inconvenience. The practicability of apportioning a tax implies some measure of elasticity. Apportionment, however, is possible only in the case of certain kinds of taxes. The inheritance tax is almost necessarily rated—that is, the rate is definitely fixed by law. It is hard to see how it could justly be otherwise. Very much the same thing may be said of indirect taxes.

§7. There is no one tax that is entirely satisfactory from every point of view and for this reason, if for no other, a system of taxation is better than any single tax. If it were necessary to rely on one tax exclusively, an income tax would doubtless be the best, though it would be far from satisfactory.[3] Even if such a tax were made progressive, it would not allow for differences in taxpaying ability, for ability does not depend merely on the size of one's income. Much depends on necessary expenses, which are not the same for all persons. Some allowance may, indeed, be made for dependents, but this meets the difficulty only in a rough and partial way. A man's necessary expenses depend, in part, on the circumstances under which he lives and works, on his health, on the cost of living in the community, and on the profession, trade, or business in which he is engaged.

[3]For a fuller discussion see Seligman, "The Income Tax," pp. 15ff.

Something should be allowed for savings against old age or other disability. The source of income is not a matter of indifference. A secure, permanent income, independent of the exertions of the recipent, represents a larger degree of ability than does a precarious one, and personal earnings are more or less precarious. The receipts from an inheritance may properly be regarded, at least in the case of collateral inheritances, as giving a special measure of ability. Indeed, it would be difficult to enumerate all the circumstances that should be taken into account.

If public expenses were so small that only a very moderate rate of taxation need be imposed these inequalities might be regarded as a negligible matter. In fact, however, the burden of taxation is heavy, and in all probability it will continue to be so. The benefits resulting from public expenditure may far outweigh the cost, but the cost is so great as to make its just distribution a matter of importance. In a properly devised system of taxation sources of ability will be reached that cannot be reached by any one tax. As a consequence, where each tax is but a part of a system its faults will be less severely felt than if it were the sole source of public revenue. It is unlikely that the inevitable faults of each tax will injuriously affect the same individual.

There is one other weakness of any single tax that must be taken into account. As the rate is increased, the temptation to evasion becomes stronger, and the administration of the tax more difficult. The man who will cheerfully submit to assessment for a tax that will take only one per cent of his income will generally be more reluctant when the rate is five per cent. When it reaches ten per cent evasion, and perhaps perjury, are likely to be common. Before it reaches twenty per cent administrative success, in most cases, at least where the tax cannot be shifted, is hardly to be expected.[4] Even in the case of land, which cannot be hidden, there is the serious problem of valuation. Where a system comprising a number of taxes is used this difficulty is greatly reduced. The gain to be derived from the evasion of any one tax is relatively small.

§8. Any discussion of reliance on one tax would be incomplete, especially under the conditions existing in Washington, without some reference to the single tax on land values or land rent.[5] Now it

[4]A property tax of 20 mills on full value (or 40 mills on a fifty per cent valuation) would, if the property yielded the very high return of ten per cent, be a tax of twenty per cent on the income from that property.

[5]For a much more extended discussion see Seligman, "Essays in Taxation" (eighth edition), Ch. III.

should be clearly realized that the proposal of Henry George and his followers is not primarily a fiscal matter, but a fundamental social reform, a panacea for all social ills.[6] It rests upon the theory that private property in land is wrong. Single taxers do, indeed, make much of the fact that they do not propose to do away with the private use of land or legal title to it. They would simply take the entire economic rent. In other words, they would allow the form of private ownership to remain, but the "owner" would really be in the position of a tenant having a transferable lease indefinite in duration, but with the rent subject to frequent adjustment by the state. Among the specific evils from which they believe our social ills flow are the withholding of land from use, speculation in land, and the receipt of an unearned income.

There are, however, many who call themselves single taxers who do not go to the same lengths as Henry George, either in their proposals or in their anticipations of results. They look at the matter more largely from a fiscal point of view, though ordinarily the idea of social reform is not absent, and in many cases it is strong. They would not necessarily confine taxation to land values nor would they take the entire rent. In some cases their position is less one in favor of the single tax than in opposition to inequalities and injustices of the general property tax.

With the single tax as a social reform we are not here concerned, and anything like an adequate discussion of it would carry us far afield. If the theories of Henry George and his followers be correct—and that they are even substantially correct very few, if any, recognized economists believe—their proposals should, of course, be adopted. This would, perhaps, make real taxation unnecessary, for the state would, in effect at least, become the owner of all the land and would receive rent. If the more moderate "single taxers" be right—and even this is not here admitted—a combination of social reform with taxation may, perhaps, be justified. The result, however, would not be the single tax.

[6] "What I, therefore, propose as the simple yet sovereign remedy which will raise wages, increase the earnings of capital, extirpate pauperism, abolish poverty, give remunerative employment to whoever wishes it, afford free scope to human progress, lessen crime, elevate morals, and taste, and intelligence, purify government and carry civilization to yet nobler heights, is—**to appropriate rent by taxation.**" George, "Progress and Poverty," Bk. III., Ch. II. For a recent, but less sweeping view, see Bolton Hall, "Taxation of Land as a Remedy for Unemployment," Annals of the American Academy of Political and Social Science, Vol. LIX. (May, 1915), pp. 148-156.

The idea that the income from land is unearned is so widely held that a few words of comment are desirable. In the opinion of the author, the idea contains some truth, though not nearly as much as is sometimes supposed. So far as the income is unearned it may be regarded as furnishing a special measure of ability which may very properly be subjected to taxation. In this respect, however, the income from land does not stand alone. There are a number of social institutions and conditions from which individuals receive a benefit that is, in much the same sense, unearned. Inheritance, particularly in the case of collateral relatives, is one of these. It is only by a great strain of language that certain incomes from natural monopolies can be brought under the single tax. These are but a few of the most obvious instances. If we were to examine the meaning of the term "earn" it is quite possible that we should come to the conclusion that there are substantially no incomes that are not, at least in part, unearned. Even if the term be not taken so broadly, however, the attempt to reach the unearned incomes only would result in a somewhat complicated system of taxation; but ability, however great, if it rested on earnings, would be exempt.

It must not, of course, be inferred that land values are not one very good subject for taxation; and, as we shall see there are very few subjects in the State of Washington that are today more heavily taxed. Neither must what has been said in regard to the single tax on land values be taken as a defense of the existing system.

§9. A system of taxation might well contain a number of taxes that, considered by themselves, would be far from satisfactory. Taxes that, used alone would be very unequal in their operation might be so combined as to secure a substantially just result. It is not necessary that every tax be elastic. There are many which are weak in this respect, but very good from other points of view. There are other taxes that are well suited to securing the necessary elasticity. Even indirect taxes may properly be used to a limited extent. They can generally be so imposed as to satisfy fairly well the canons of convenience, certainty, and economy. Confined to a proper place in the system they do not necessarily offend grievously against the canon of equality. As a practical matter they can sometimes be used to reach certain cases of ability that cannot well be reached by any other method.

The tax system should be composed of a number of taxes so chosen that the unavoidable defects of each will, so far as is prac-

ticable, be offset by one or more of the others. The end should be to tax each person sharing in the benefits of the state according to his ability. No one tax should be so heavy as to put an undue strain on the administrative machinery. It is sufficient, as regards some taxes, that they be steady and reliable. Others should be readily capable of adjustment and these—at least so far as unlimited democracy is desirable—should be universal in their application and of such a character as to make clear to the voters the relation between public economy and the burden of taxation.

Chapter III.

THE GENERAL PROPERTY TAX:

Scope; Levy; and Collection

§1. By the "general property tax" is meant a tax upon the owners of property in proportion to its value. There may be a few exemptions and a few kinds of property may receive special treatment, but these are merely exceptions to the general rule. Aside from these the rate is the same whatever the kind of property held. Where property is divided into classes on which different rates are imposed we have a classified, rather than a general, property tax. Sometimes we hear of a progressive general property tax, under which the rate increases with the amount of property held by one taxpayer. In this country the rate is the same whatever the amount of property, save only that in some cases there is a moderate exemption. The exemption does, indeed, give the tax a somewhat progressive character; but the effect is so slight that there is no substantial inaccuracy in saying that the tax is proportional rather than progressive.

§2. The taxation of property is one of the oldest and, historically at least, one of the most widespread forms of taxation. It is said that the general property tax, or something closely resembling it, has been tried in every civilized country existing today.[1] As one of the chief sources of revenue, however, it has been abandoned in nearly all of them, though it still survives in Australia, in some of the Swiss cantons and, at least as a local tax, in most of the American states. The working of the general property tax has been repeatedly examined in many places by tax commissioners and by academic investigators. With an approach to unanimity that is rarely attained in such important matters of governmental policy they have condemned it as unjust, and impossible of administration in accordance with the intent of the law.

It need not be supposed that the general property tax was always as unjust and impractical as it is today. Many of the American states in which it still exists adopted it in their infancy, some of them while they were still British colonies, though ordinarily it was associated with a poll tax. In New England it developed from a real property

[1]For a discussion of the general property tax in history, as well as in its present day working and in theory, see Seligman, "Essays in Taxation (8th edition), Ch. II.

tax and was supplemented by a "faculty tax" designed to reach those whose ability to pay depended on earnings from personal exertions rather than on the possession of property. In most, if not all, of the states at the time of their adoption of the general property tax economic conditions were relatively simple; the expenses of government were comparatively small; property consisted, for the most part, of land and of goods that were locally owned, easily found, and easily valued; there were few, if any, great business corporations; and the distribution of wealth and of income were much more nearly equal than they are today. Under such conditions the general property tax was a natural and, upon the whole, a simple one. The difficulty of assessing certain kinds of personalty, however, was felt almost from the first; and in Massachusetts, as early as 1651, we find a special attempt, which apparently was not very successful, to deal with the property of "marchants, shopkeep.s and factors."[2]

§3. At the time when a territorial government was organized in Washington the general property tax was the form of taxation most used by the states. It is therefore not surprising to find in the organic act, passed by Congress in 1853, the provision:

"And all taxes shall be equal and uniform; and no distinctions shall be made in the assessments between the different kinds of property, but the assessments shall be made according to the value thereof."[3]

Under this provision the Legislative assembly, at its first session, held in 1854, passed an act for the taxation of property "valued in equal and rateable proportion." Exemptions were allowed in the case of religious societies, benevolent, charitable, literary, and scientific institutions, the territory and its counties, school houses and school lands, public libraries, places of burial, and Indians.[4] As was commonly the case elsewhere, the property tax was associated with a poll tax, but it was provided that this should go to the county.

Since the passage of this act the primitive frontier territory with a population, at its first census, of 11,594 has grown to a great, highly organized state with a population, at the last census, of 1,141,990. The simple economic conditions have given place to conditions of great complexity. Wealth has multiplied many times in amount; it has assumed a vastly enlarged variety of forms; and the inequality in its distribution has increased. Great railroads have been built, mak-

[2]Seligman, loc. cit., p. 23.
[3]I, "Laws of Washington," p. 36.
[4]Ibid., p. 331.

ing it possible to maintain close business and social relations with the rest of the country. Among the producers of wealth are large corporations, some of which have their headquarters and much of their property in other states.

Amid all these changes the chief element in the tax system has, in its fundamental character, remained unaltered, save that by statutory definition credits of various sorts are not property for purposes of taxation. The constitutional provision which replaced that of the organic act is somewhat more elaborate and rigid in form, the right of exemption being narrowly limited, but it is otherwise substantially the same. The one amendment that has been passed permits the exemption of personal property to an amount not exceeding $300 for each head of a family. The law has been made more precise by statutes and by judicial decisions, and administrative methods have been considerably developed; but with the important exception of the treatment of credits, it is still the general property tax that is so widely condemned by the recognized authorities.

To some it will doubtless appear that this condemnation is unwarranted. Granting that different principles may properly be adopted under different types of civilization, there is no sufficient reason why a principle, fundamentally sound, should be abandoned because the social organization has become large and complex. All that is needed is that the application of the principle be made effective. This may require more highly developed administrative machinery than has yet been used; but it does not justify a modification of the principle.

What is overlooked is the fact that the taxation of all property at a uniform rate is not so much a principle as a method. The fundamental principle is that each person sharing in the benefits conferred by the community should pay taxes according to his ability. It must be remembered that it is not property that has obligations and pays taxes, but men and women. Other things being equal, it is upon its success or failure in imposing taxes according to ability that the general property tax must stand or fall. If the object sought can be more readily attained by a modification of the general property tax, the modification should be made. If without introducing evils greater than those for which a remedy is sought an entirely different system would be more effective, the general property tax should give way to it. Even if the former could be well enforced, the question would still

remain as to whether property, without regard to its form, is a satisfactory test of ability. It is the principle that is of vital importance, not the method.

We have then to consider the general property tax in its actual working in the State of Washington today. It is not enough to know that it is condemned by tax commissions and by professional students of economics. If the people are to deal intelligently with the subject of tax reform they must know what the present system is and where lie its merits and defects. It should be said, moreover, that the almost unanimous condemnation that is heaped upon it is not a condemnation of the taxation of property, but of the attempt to tax all kinds of property and that at a uniform rate. Many of its severest critics would retain a considerable part of it, but would tax certain kinds of property at special rates, and would deal with other kinds by entirely different methods. It is not their object to give favors to any class of taxpayers, but to establish a system which will, in fact, require each to pay according to his ability.

§4. The State Constitution provides that all property in the State, not exempt under its provisions or by the laws of the United States, shall be taxed at a uniform and equal rate according to its value.[5] This at once raises the question of what property is. In regard to land and other material goods there can be no question: so long as anyone has a just claim to their possession they are property. In addition there are certain legal rights that are included under the term. "Royalties and patent rights" is one item in the list of taxable personalty. "Leaseholds" is another. The franchises of public service corporations have been held to be property. The "good will" of a business, however, is not ordinarily so regarded, although it receives legal protection, may be bought and sold, and is sometimes very valuable.[6]

There is probably nothing ordinarily subject to taxation that has been a source of more difficulty in the administration of the general property tax than what are commonly called intangibles. Under this head are to be included stocks, bonds, mortgages, bank deposits, and, in fact, practically all forms of credit. For a long time the attempt was made in Washington, as in other states where the unmodified general property tax exists, to tax these as material forms of property are supposed to be taxed; and, as in other states, the result was

[5]Article VII, Sections 1 and 2.
[6]For a discussion of this point see below, pp. 68 and 83.

distinct failure.[7] In 1907 the legislature inserted in the law the clause: "Provided, That mortgages, notes, accounts, moneys, certificates of deposit, tax certificates, judgments, state, county, municipal and school district bonds and warrants shall not be considered as property for the purpose of this chapter, and no deduction shall hereafter be allowed on account of indebtedness owed." The effect of this proviso is to exempt credits of practically all kinds, including corporation securities.

It does not follow that the legislature is free to define property in an arbitrary manner. In passing on the constitutionality of the exemption the Supreme Court held that money is clearly property and, as such, must be taxed. Credits, too, are property in a sense, but they have a representative character. Taking a loan as an example, the Court remarked[8]:

"The credit in the hands of B is a matter of no value of consequence except for the prospect or faith that A will in the future deliver to B $5,000 in actual money or other property. That money or property that may in the future come to B is still in the hands of A or someone else from whom A will procure it; and meanwhile it is taxed at some place, wherever it may be, no matter who possesses it or controls it, whether within or without this state."

In upholding the constitutionality of the exemption, except as regards money, the Court laid much emphasis on the fact that the taxation of intangibles results in double taxation. Even if this is not

[7] In 1906, the last year in which a general attempt was made to reach property of this sort, the total amounts assessed were as follows:

Money and credits of banks, bankers, brokers, etc.	$ 4,857,482.
Moneys on hand or on deposit	3,151,452
Notes, accounts, tax certificates, warrants and other credits	3,016,960
Bonds, stocks and shares	709,030
Total intangibles	$11,734,924
Total personal property	$ 82,151,507
Total property, real and personal	530,209,882

In commenting on the exemption of intangibles the State Board of Tax Commissioners remarked: "The value of intangible personal property in the State probably exceeds by several million dollars the total value of all property now on the tax rolls. * * *." ("Second Biennial Report, p. 47.") This is possibly an overestimate; but even if the amount of intangible were equal only to the amount of tangible personality, it is obvious that but a small percentage of it was reached; and a very large proportion of that was in the hands of "banks, bankers, brokers, etc." The property of domestic corporations, other than banks, was by law assessed to the corporation itself, and the stock was not assessable to the stockholder (Ridpath v. Spokane Co., 23 Wash. 436). Even allowing for this, the item of $709,030 for "bonds, stocks, and shares" seems ridiculous.

[8] State ex rel. Wolfe v. Parmenter, 50 Wash. 164. This decision contains a very good discussion of the principles underlying the exemption. The dissenting opinion of Justice Fullerton contains a good discussion of the opposing view. It is interesting to notice that Justice Fullerton took the case of stocks and bonds of a railroad whose tangible property lay without the State, as an example of what he regarded as the unfortunate effect of the decision.

forbidden the law should not be interpreted so as to require it. The constitution makes it just as imperative that the taxation of property shall be uniform as it does that all property shall be taxed, and the Court remarked that it was a matter of common knowledge that the attempt to tax credits was one of the most fruitful sources of inequality in taxation, and the legislature doubtless had this in mind when it passed the law.

There was one other case in which the attempt was made to grant relief from taxation by definition. The statute provided that ships and vessels registered at any custom house within the state, but engaged exclusively in interstate or international trade were not to be listed for taxation, "such vessels not being deemed property within the state." In a very recent decision this statute has been declared unconstitutional, it being held that the situs of the vessel was actually within the state.[9]

§5. As cases of this sort show, the right of the legislature to make exemptions is narrowly limited. The following are the clauses of the Constitution dealing with the subject[10]:

"Provided, That a deduction of debts from credits may be authorized: Provided further, That the property of the United States and of the State, counties, school districts and other municipal corporations, and such other property as the Legislature may by general laws provide, shall be exempt from taxation; and provided further, That the Legislature shall have power, by appropriate legislation, to exempt personal property to the amount of $300 for each head of a family liable to assessment and taxation under the provision of the laws of this State of which the individual is the actual *bona fide* owner."

It will be noticed that public property—federal, state, and local—is alone specifically exempt. Quite apart from its own constitution a state has no power, without the consent of Congress, to tax federal property or the lands of Indians living in tribal relations. Even for the taxation of national banks such consent is necessary; but this, subject to some restrictions, has been given. The exemption of the property of the state and its subdivisions means simply that one branch of the government shall not have power to tax another branch. In some cases this would be of considerable importance. Thurston County, for example, might draw revenue from the rest of the State by reason of the fact that Olympia is the capital. On the other hand, cities already heavily burdened would be required to pay taxes to the

[9]Pacific Cold Storage Company v. Pierce County, 85 Wash. 626.
[10]From Article VII, Section 2.

state. The principle, however, that governmental agencies shall not be subject to taxation is well established in this country.

§6. Besides the property which the Constitution definitely ordains shall be exempt there are a few cases in which discretion is given to the legislature. Specifically mentioned are the deduction of debts from credits and the exemption of $300 worth of personal property for each head of a family. Since credits are no longer property for the purpose of taxation, the statute permitting the deduction of debts from credits has lost all meaning and has been repealed. Provision has been made, however, for the exemption of $300 worth of personal property for each head of a family and for widows; and this gives the tax a certain progressive character which is not of much consequence unless the amount of property held is small. Those who favor a tax on bachelors, however, should notice that the effect of the exemption is to place on single persons a property tax of limited amount, which is not laid on other members of the community. This tax, if the rate were forty mills, would be limited to $12 a year. There would, indeed, be a few cases in which the tax would fall on married persons, such, for example, as a wife who was taxed separately from her husband.

In the second exemption clause quoted above appear the words: " * * * * and such other property as the legislature may by general laws provide, shall be exempt from taxation." If these words be taken from their context they seem to give the legislature a free hand. As a matter of fact they are a part of the clause exempting public property. It has been held,[11] in accordance with a well understood principle of legal interpretation, that they refer to property of the same general kind: that is, to public property, or to property which, while privately owned partakes of a public nature, such as that of educational, religious, and charitable institutions. It was because of this decision that a constitutional amendment was necessary to permit the exemption of $300 worth of personal property for each head of a family.

A number of exemptions have been granted which seem to be in harmony with the decision. The list is quite long. It includes: public burial grounds and cemeteries; churches built and supported by donations whose seats are free to all; non-sectarian religious societies,

[11]State ex rel. Chamberlain v. Daniel, Assessor, 17 Wash. 111. This decision was the result of an attempt on the part of the legislature to allow an exemption of $500 personality and a like amount for improvements on land.

organized chiefly for religious purposes and not for profit, together with their properties used for educational, benevolent, and social protective purposes arising out of their religious work, where these are for the public good; hospitals, orphanages, institutions for the reformation of fallen women, and homes for the aged and infirm, supported in whole or in part by public or private gifts; humane societies to an amount not exceeding $10,000; free public libraries; art, scientific, or historical collections, where they are maintained and exhibited for the benefit of the general public and not for profit; schools and colleges supported in whole or in part by gifts, endowments, or charity, the annual income of which from endowments is at least equal to that from tuition fees; fire engines, etc., and the buildings of fire companies when owned by them; and certain fraternal societies on property other than real estate and office furniture. Nearly all of these exemptions are subject to limitations and to provisions designed to prevent abuses. The amount of land that shall be exempt is, in many cases, limited. Usually the property must be used exclusively for the purposes of the particular organization on account of which it is exempt. In some cases the State reserves the right of inspection or even the right to a place on the board of trustees, *ex officio,* for certain public officials.

§7. In a few cases provision has been made for exemption by statutes which would seem to be unconstitutional. For a long time all fruit trees, except nursery stock and forest trees artificially grown, were declared to be exempt. As a matter of fact, the assessors seem to have paid little attention to this provision except to urge that it be repealed. Fruit trees were not, indeed, taxed as trees, but as a part of the land on which they grew. As one assessor put it, "an acre of land with a full bearing apple orchard is worth on the market, say $800 to $1,500 per acre according to location, water right, distance from transportation and other causes."[12] This method of assessment had the approval of the State Board of Tax Commissioners, which regarded the exemption as unconstitutional. In 1912 the county assessors, in their annual convention, adopted a resolution, the language of which is significant, at least as showing the opinion of the committee by which it was framed, "that that section of the law *purporting to* exempt fruit trees from assessment and taxation

[12]B. F. McCurdy, "The Basis and Equalization of Assessments," Proceedings of the Fourteenth Annual Convention of County Assessors (1912), p. 28. Hereafter these publications will be referred to simply as "County Assessors," preceded by the appropriate number.

should be repealed."[13] The exemption was removed from the statute in 1915.

There still stands an act providing for the exemption of "all ships, vessels, and boats in actual construction and all materials especially designed and set apart for them." However desirable this measure of protection to a state industry may be, it is hard to see how it could stand the test of constitutionality if the question were raised. In practice the assessors seem to allow the exemption; and the matter has not been brought before the courts.

§8. The amount of revenue secured by the general property tax and, in so far, the weight of the burden upon the taxpayer, depends chiefly on the amount of public expenditures. It is, of course, true that there are other taxes by which revenue is secured, but the rate at which they are imposed is definitely fixed for considerable periods of time, and is not ordinarily varied to meet the fluctuating needs of the government. The general property tax is the elastic element in the revenue system; and it is consequently the tax the rate of which is directly connected with appropriations.

One way in which the attempt is made to keep down the rate is by the use of statutory limitations. Various "funds" which can be used only for specified purposes are established in the treasury, and, with a few exceptions, the rate that may be imposed for each is limited to a certain number of mills. In the case of counties, cities, etc., such maxima, being fixed by the State, are legally binding. In the case of the State itself, however, the legislature that imposes a tax may raise the limit or may establish new funds. Any limits it may fix are, of course, binding on the administrative officials. As regards the Legislature the chief effect of the rate limitations is to give special cause for consideration of the total rate that appropriations may make necessary.

The existence of some of these funds is required by the Constitution and even by the "enabling act" under which statehood was conferred. In some cases the chief reason for the funds seems to be that there are certain revenues that can be used only for certain purposes. For example, the enabling act provides that five per cent of the receipts from public lands sold by the United States, less expenses, shall be paid to the State, "to be used as a permanent fund, the interest of which only shall be expended for the support of common schools." In some cases a motive for the creation of certain

[13] 14 County Assessors, p. 13. Italics are the author's.

special funds is to give expression to a permanent financial policy in regard to the amount of taxes that shall be levied for certain purposes. Such, for example, are the State University fund and the funds for the other institutions of higher education. Another reason, doubtless, is need of the State for increased revenues in the face of the statutory limit of three mills for general state purposes. It would, of course, be legally possible to raise this limit; but this would appear to many to open the way to increased extravagance, though they may be willing to be taxed for the purposes represented by the special funds. It should be noticed that the total state tax very considerably exceeds the limit on taxes for general purposes.

§9. Except as regards certain special funds for which definite rates of taxation are provided, the general property tax is as an apportioned tax. The legislature determines the amount of money to be raised, but does not directly fix the rate. That cannot be done until the total value of taxable property has been ascertained. As it is in the assessment and equalization of the tax that the fundamental practical defects are to be found, we shall examine these phases of the subject later in some detail. Here it is sufficient to note that it is not until equalization has been completed that the rate can be determined.

The county boards of equalization begin their sessions on the first Monday in August, and the state board on the first Monday in September. The county boards meet again in November and April, but only for the correction of certain kinds of errors, not for equalization purposes. After the state board has completed its work of equalization it apportions the amounts to be raised by the various counties for state purposes, including those for which permanent provision has been made, such as interest and sinking fund requirements, on the basis of the valuation as equalized by itself. Within ten days after its adjournment, the state auditor, who is ex *officio* its president, sends to each county assessor a transcript of its proceedings, specifying the amount—not the rate—to be levied in his county for state purposes.

§10. The assessor, having now all the necessary data in his possession, proceeds to calculate the rate of the tax on the assessed value as fixed by the county board of equalization. Since the amount of the state tax apportioned to each county is based on the state equalization, the burden of the tax on the different counties is as nearly uniform as possible; but since the rate is calculated on the basis of the county equalization, which is rarely the same for any

two counties, the rate of the state tax varies from county to county, being high where property has been assessed at a low valuation and low where a high valuation has been made.

To the rate for state purposes must be added the rates for county, municipal, school district, road district, and other local purposes. The amounts of these taxes, or in some cases the rates, are certified to the assessor by the proper officials, not later than the tenth of October, in much the same way as the amounts for state purposes are certified by the state auditor. The assessor then proceeds to the "extension" of the tax, which means simply the entering in the assessment books, opposite each description of real property, or, in the case of personalty, opposite the name of the taxpayer, the amount of taxes levied.

The extension of taxes being completed, the assessor makes out and sends to the state auditor an abstract of the rolls, showing the number of acres of land assessed and their value, including that of structures; the value of the taxable personalty; the totals; the totals as equalized; and the amount of taxes for all purposes for that year. Not later than the fifteenth of December, he turns the books over to the county auditor, entering in each his certificate that the list is correct. The auditor attaches his warrant authorizing the collection of taxes and on the first Monday in January sends the books to the county treasurer, charging the amount of taxes against him. The journey of the assessment books is now ended; and after they have been used by the treasurer they are preserved as public records in his office.

§11. The collection of all taxes, whether state or local, is in the hands of the county treasurer. The methods of collecting taxes on real and personal property differ in some respects; but as regards both much more consideration is given to the convenience of the taxpayer than is the case in some other parts of the country. The fact that there is an advantage in having but one collector of taxes does not seem to be everywhere realized, though it would seem to make for economy as well as for convenience. The taxpayer receives but one bill for his real and one for his personal property in the county. He does not have to appear in person at the treasurer's office, but may make payment by mail; and cheques drawn on banks within the county are commonly accepted.

Upon receiving the assessment books from the auditor the treasurer makes the proper entries in his own books, adding to the current

levy the amounts of any taxes that may be delinquent. As regards real property notice is given by publication, once in each of three consecutive weeks, that the books have been turned over to him for the collection of taxes. Notice of taxes on personal property must be sent by mail to each person assessed; and, upon request, the treasurer is required to notify the taxpayer of the total amount of taxes on real property due from him, with a statement of the name of each tax and the rate of levy made upon it. In practice, in some counties at least, simple bills for taxes upon real and upon personal property are sent to each taxpayer. The collection of taxes begins on the first Monday in February, and the treasurer is not permitted to accept any payment before that date, except in the case of property about to be removed from the county and in the case of "itinerant merchants."

§12. Taxes on personal property do not become delinquent until March fifteenth. If they are not paid by that time the treasurer is required to make a special effort to collect them, and failing in that, to notify the sheriff, whose duty it is to distrain sufficient property to pay the taxes, together with all costs and interest at fifteen per cent per annum, posting notice of sale not less than ten, or in the case of standing timber,[14] fish trap locations and certain kinds of fish net locations not less than thirty days later. If payment is not made within that time the property, or as much of it as may be necessary, is sold at public auction. If any surplus remains from the price received it is paid to the former owner of the property. Personal property taxes constitute a lien against all real and personal property of the assessed.

The treasurer is personally responsible for wilful refusal or neglect to collect the taxes on personal property; and the law requires the deduction of the amount from his salary. If, however, he is unable to collect, by distress or otherwise, he files with the county auditor, on the first of January, a list of the taxes, with an affidavit made by himself or the deputy to whom the matter has been entrusted, to the effect that he has made diligent enquiry and search for goods and chattels on which to levy, but has been unable to collect.

An interesting case of distraint arose in Seattle in 1910 when the treasurer of King County, after failing to collect from the Seattle Electric Company delinquent taxes amounting to about $167,000, proceeded to distrain a hundred and twenty-five street cars and some

[14]Standing timber, when owned separately from the land, is personality.

trackage, and for a time a tie-up of the system was threatened.[15] The delay in the payment of the tax arose out of a disagreement as to the taxable value of the franchise, the company saying that it had no desire to refuse payment of the amounts justly due from it. The company promptly tendered payment of the taxes and costs, without interest; and this was accepted. As the interest would have amounted to $30,000 the treasurer was subjected to some criticism; but his position was upheld in opinions given by the prosecuting attorney of the county and the attorney general of the State. Owing to a defect in the law, the interest could not be collected unless the case was actually carried on to a sale. The defect in the law has since been corrected.

While ordinarily notice of the amount of personal property taxes due must be given, they may be collected without notice if, after they have been levied, the treasurer learns that the property in question is about to be removed from the county. If, at any time after assessment, but before the levy, either the assessor or the treasurer learns that property is about to be dissipated or removed from the state the law requires the adoption of a similar policy, the rate in this case being computed on the basis of the levies for the preceding year. If, however, the property is merely removed to another county after assessment, but before the levy, the treasurer of that county is notified, and it is his duty to collect the tax and turn the proceeds over to the treasurer of the county in which it was assessed, deducting the cost of collection. Delinquent taxes and penalties are treated in the same way. While provisions of this sort for dealing with propery that is about to pass from the jurisdiction of the county may be of some use in conspicuous cases, it is difficult to see how they can be given a general application in a country in which there is as little supervision of the comings and goings of the individual as in this.

There is one other case in which taxes may collected earlier than at the regular time. This is the case of "itinerant merchants," or persons, firms, or corporations who bring goods into the State after the date of assessment, and open a temporary place of business in which to sell them, without the intention of being permanently engaged in trade. Such persons are required to notify the assessor, who then determines the value of the goods, and taxes are collected at the rate for the current year. Failure to notify the assessor renders the owner liable to a penalty of double the amount of the tax.

[15]For details see Seattle daily papers for May, 1910.

§13. As has already been stated, the methods of collecting taxes on realty differ somewhat from those used in the case of personalty. In both cases, however, collection begins on the first Monday in February. Taxes on real estate, however, do not become delinquent until the thirty-first of May; and when the total amount owed by one person is as much as $2 he need pay only one half of it at that time, postponing payment of the remainder until the thirtieth of November. If payment is not then completed the unpaid half becomes delinquent and interest, at the rate of fifteen per cent per annum, is charged from June first. On the other hand, if the full amount owed by one person is paid at one time on or before the fifteen of March a rebate of three per cent is allowed.

Taxes, including, if delinquent, interest and costs, constitute a lien against the property on which they are imposed prior to other forms of obligation. They do not, however, constitute a personal lien against the owner. Arrangements have been made to permit the payment of taxes by anyone who has a legitimate interest in the property, with the right to recover the amount of the payment from the owner.

After taxes have been delinquent for one year the treasurer sells to anyone applying, a certificate of delinquency, the purchaser paying the amount of the tax, and being entitled to interest at fifteen per cent. For this certificate a fee of fifty cents is charged. At any time previous to the issuance of a tax deed the property may be redeemed, and all claims against it released, by the payment to the county treasurer, for the benefit of the holder of the certificate, of the amount for which it was sold, with interest, and the amount of penalties, interest, and costs paid by the holder of the certificate, and interest upon such payments. No fee, however, is charged for redemption.

After three years from the date of the original delinquency, if the property has not been redeemed, the holder of the certificate may serve notice upon the owner, by publication if necessary, summoning him to appear and defend an action for foreclosure, or pay the amount due. A copy of this notice must be filed with the county treasurer; and if anyone interested in the property seeks to redeem it the costs of foreclosure, as ascertained by the treasurer, are added to the price of redemption.

Before applying for judgment the holder of the certificates must see to it that all taxes accrued on the property to date have

been paid. If he fails in this a second certificate may be issued, and the holder of the first forfeits all his rights to the holder of the second, receiving from him, however, the price of the first with interest. These provisions, however, do not apply where the holder is a county or a municipality, since such holders are not obliged to pay back taxes until the property is sold, and then the proceeds of the sale must be justly apportioned among the different taxing districts.

The law provides for the placing upon the county of most of the expenses incident to foreclosure by the holder of a certificate. The county itself, upon request, prosecutes the action to final judgment, the holder paying a court fee of $2. If he so desires, he is at liberty to employ counsel of his own to work either with the prosecuting attorney or independently. The prosecuting attorney, however, is not permitted to collect any fee for his services.

A full discussion of the legal aspects of foreclosure would require a volume in itself, and would be out of place in a work of this kind. One or two points, however, may be noticed. When the property is sold for taxes only as much as is necessary to raise the required amount is sold. The property may be redeemed at any time before the deed is executed; and in the case of minor heirs or insane persons it may be redeemed at any time within one year from the removal of the disability upon payment of interest on the purchase price at fifteen per cent per annum, and a reasonable compensation for improvements made in good faith, less the value of use. If the land has been sold for taxes to which it was not properly subject or taxes which have been paid, the treasurer is required to make entry on the sale or redemption record that the land was erroneously sold, and this entry is *prima facie* evidence of the fact. From these cases alone it will be seen why a tax deed is commonly regarded by a purchaser as not entirely satisfactory.

At the end of five years from the date of delinquency, if no certificate has already been issued, the treasurer is required to issue one to the county and to start action for foreclosure. The legal proceedings in this case are practically the same as when action is brought by an individual. Summons may be served and notice given, however, in one general notice. All the certificates issued at the time may be combined in one book and one action brought, all persons interested being made co-defendants. The persons whose names appear on the treasurer's books as owners are regarded as such.

§14. At the last session of the legislature an attempt was made to bring about a reduction in the fifteen per cent interest charge on delinquent taxes. Regarded as a rate of interest, fifteen per cent is undoubtedly high; but it is not merely as a rate of interest that it should be regarded. It is a penalty, designed to prevent the owners of property from allowing taxes to become delinquent. That a penalty of some sort is desirable would seem to be beyond question. The State and its subdivisions are not in the banking business. To allow taxes to become delinquent means delay in securing the public revenues; and since the government must be carried on this, if done on a large scale, means public borrowing. In practice such borrowing, whether or not the difficulty was due to delinquency in the payment of taxes, has not infrequently been done by what amount to forced loans. Warrants have been issued against which there were no funds in the treasury. Government employees do not ordinarily wish to invest their wages in public securities; nor do other creditors, as a rule, wish to hold warrants. To adopt a practice of placing upon them the responsibility of securing cash, especially if, as sometimes happens, the warrants will be accepted elsewhere only at a discount, is bad business and bad public finance, not to say bad public morals.

It is said that before the passage of the law requiring fifteen per cent interest a very large proportion of the taxes commonly became delinquent; and in deciding on the amount of tax levies allowance was made for the fact that taxes would not be paid promptly.[16]

It may be thought that the government has at least good security for the eventual payment of the amounts due; but it would seem that, in practice, delay has sometimes meant serious loss. It appears that before the fixing of the high interest rate, there were taxpayers who would allow their taxes to become delinquent for a term of years, and when any move was made to compel payment would appear with a proposal for a compromise on the basis of a certain per cent of the tax, without interest. The treasury being in need of funds, the county commissioners would accept the offer. One case is cited in which a corporation was able to save $50,000 in this way at the expense of the other taxpayers.[17] This was doubtless an

[16]F. E. Jones, "Tax Delinquent Certificates,' 14 "County Assessors" (1912), p. 55.

[17]Ibid., p. 56.

extreme case; and the practice might have been prevented in some other way than by the charging of a high rate of interest. It illustrates, however, a way in which delay in payment may result in eventual loss.

As regards the hardship of the interest rate it must be remembered that the taxpayer knows, roughly, what he will have to pay long before the time for payment arrives. Early in February he learns the exact amount. The tax is not deliquent until the end of May, and even then, in the case of real estate, unless the amount to be paid is very small, half of the payment may be postponed until the end of November.

There are doubtless special cases in which the fifteen per cent interest charge works a real hardship; and it is true that, so far as possible, the public should be a reasonable creditor as well as a good debtor. If a charge of less than fifteen per cent would be sufficient to deal with substantially all cases not worthy of special consideration a lower charge should be imposed; and if a better plan of accomplishing the desired end can be devised it should be adopted. If it be decided that the State should make a practice of lending to individuals the amount of their taxes, provision should be made to enable it to pay its own debts when due. Upon the whole it may be doubted that the fifteen per cent charge is too high.

§15. It will be noticed that the collection of taxes, not including those that are delinquent, takes nearly two years from the preliminary work of assessment to the final payment. The tax bills that will be sent out next February are based on the assessment made last March. In the case of personal property payment must be made by the fifteenth of next March, while in the case of most real property payment need not be completed until the end of the following November.

Chapter IV.

THE GENERAL PROPERTY TAX:

County Assessment; General Aspects

§1. Most of the work of assessment for the general property tax is done by the county assessors under the supervision of the State Board of Tax Commissioners. The latter, however, itself attends to the very important work of the assessment of the operating property of railroad and telegraph companies, including interurban and street railways. Property of this sort is largely intercounty in character, and for that reason, if for no other, a central assessing authority is desirable. There are, however, a number of other forms of property having a similar intercounty character that are left to the care of the county assessors.

§2. The system under which the county is made the assessing district is by no means universal in the United States, and even in Washington there are a few exceptional cases. In many parts of the country, particularly in New England, a smaller unit is adopted. Commonly it is the township, and in some cases it is a single ward in a city. In each of these districts, however small, there is an assessor or a board entrusted with the work. In some states these local assessors are subject to but a very small degree of central control. In others they work under varying degrees of supervision, exercised by county assessors, boards of supervision, boards of review, or some other authority. In many cases there are boards of equalization which have the power, not only to make corrections, but to exercise some degree of supervision. In a few states power is vested in the tax commissioners to remove an assessor who is unable or unwilling to do his work properly. The difficulties in the way of the exercise of such power, however, are often so great as to render it ineffective.[1] It would perhaps, be possible to adopt a system which, while retaining township assessors, subjected them to such a degree of control that the work of assessment was highly centralized; but it may be questioned whether this would really be a township system, even

[1]See the discussion of "Administrative Problems," Proceedings of the Fourth International Conference on State and Local Taxation, pp. 357-383. The proceedings of these conferences are published, with some variation of title, by the National Tax Association, or, as it was called in 1909 and 1910, the International Tax Association. Hereafter they will be referred to as National Tax Association, preceded by the number of the volume.

though the assessors were locally elected. It is, of course, the real location of power that is of importance.

The chief advantages of the small assessment district are presumably to be found in the fact that the assessor is familiar with local conditions. The chief advantage of the large district lies in the greater probability of uniform treatment and the fact that it is possible to employ a man to devote his whole time to the work at a salary sufficient to secure a thoroughly competent assessor. The relative importance of these considerations depends upon circumstances. Familiarity with local conditions may count for a great deal where property is simple in kind and owned by individuals whose interests are chiefly local in character. It loses much of its importance when among the property owners are great corporations, and economic conditions are complex. In New England the township is a very much more important governmental unit than it is in Washington; and a much larger proportion of the revenues are spent by it. Under such circumstances uniform assessments are of much less importance than they are where the various localities contribute more largely to the common expenditure. The difference, however, is mainly one of degree; and even in those sections of the country in which conditions are most favorable to local assessment the importance of central control, if not of central administration, is coming to be more generally realized.[2] The subject is, of course, more or less bound up with the policy of "home rule" which, so far as it bears upon taxation, will be discussed later.

Although the system of county assessors is the rule in Washington, it has been greatly modified in some of the counties. The people have the power to adopt a township system of government, and in Spokane and Whatcom Counties they have done so. In Spokane County, for example, township assessors are elected for those parts of the county lying outside of incorporated cities, the latter being left under the care of the county assessor. The county assesor is supposed to have supervisory powers over the township assessors; but in practice such power has been found, as it has been found elsewhere, very difficult to make effective. The result, accord-

[2]Ohio has now a highly centralized system and very remarkable results have been obtained. Even a very large amount of intangibles have been placed upon the list, though, according to Professor Lockhart's estimate, less than half of those that are legally taxable. See Lockhart, "Recent Developments in Taxation in Ohio," Quarterly Journal of Economics, Vol. XXIX (May, 1915), pp. 480-521; Peckinpaugh, "Operation of the New Centralized Tax Law in Ohio," 8 National Tax Association, pp. 127-131. It should be noticed that in Ohio the rate for all purposes is limited to 15 mills on true value. Even this is very high for some kinds of property.

ing to the State Board of Tax Commissioers, was disastrous to uniformity in assessment and equality in taxation. The instructions of the county assessor were disregarded. The townships were enabled to dodge their share of county and state taxes. The county assessor testified, under oath, that he had been forced to reduce the ratio of assessment in the cities in order to save them from unjust and unfair taxation. "The fact is," reported the Commissioners, "that for a well organized, efficient department, under the supervision of a competent official, selected by all the people of his county and who, of necessity must treat all sections alike, has been substituted a system with no head, devoid of organization and evidently serving local interests regardless of the welfare of the community at large."[8]

It should be noted that the Commissioners do not place the responsibility for the evil conditions they describe upon the shoulders of the individual assessors. There is no good reason for supposing that, in the majority of cases, these men are any more willing to be unfair than are their fellow-citizens, and certainly no charge of dereliction of duty is made. The fault is in the system.

The assessor, whatever the size of his district, holds a very important office; and it is a matter of great consequence that he be a man of considerable ability and experience, and thoroughly honest. The conditions governing the selection and retention in office of county assessors in this state are unfavorable in several respects. The office is a political one; the term for which it may be held is short; and the remuneration is small. It may be admitted, however, that as a class, the assessors seem to be men really interested in their work and desirous of doing it justly and well.

§8. The assessor, like most other county officials, is chosen at biennial elections. To many people any method of selecting public officials other than by popular vote seems undemocratic. But democracy, however, means, not that every official shall be elected, but that the government shall be really controlled by the people. Where there are many offices to be filled only the highest receive anything like the attention they deserve; and the long ballot almost necessarily results in the election of candidates whose merits the people have been unable to consider. The assessor is but one of many candidates. At the time he is chosen the people also vote for members of the United States House of Representatives, and perhaps for a

[8]Third Biennial Report of the State Board of Tax Commissioners (1910), pp. 17 and 18. Hereafter these reports will be referred to simply as Tax Commissioners, preceded by the number of the report.

Senator and for the President; for members of both houses of the State Legislature, and perhaps for the Governor and Judges of the Supreme Court; and for a considerable number of county officers. They have also to pass on initiative and referendum measures; and if present indications are to be trusted these will continue to be numerous. Under such conditions an intelligent vote on the candidates for county assessor is hardly to be expected.

The work of the assessor is almost entirely administrative, rather than political. With questions of public policy he has very little to do. It is his business to determine the value of property for the purpose of taxation, treating all property owners without fear or favor, and to show on the tax rolls the amounts to be collected from each. In determining the rate of taxation he simply makes a mathematical computation, the factors being the value of the property within his county as equalized, and the amount of taxes authorized by other officials. The "extension" of taxes is simply the application of the rate to the holders of real and personal property. Assessors are frequently blamed for high taxes, but for this they are not responsible. The most they can do is to help their counties to dodge their fair share of state taxes; or perhaps, by the use of the same methods, to protect them from similar attempts on the part of other counties. Even this is possible only so far as the State Board of Equalization fails in its work. It is the business of the assessor, not to determine public policy, but to ascertain certain facts, and to make such use of the facts as is prescribed by law. For this the qualities needed are ability, sound judgment, experience, and honesty.

Merely to make the office of assessor appointive would not, of course, guarantee the selection of the best men available. Good political machinery does not insure good government, though without it the best results cannot be attained. It is highly desirable that the responsibility for the effective working of the tax system be centralized; but only on condition that those in whom responsibility is centered are held to a strict account. If this is to be done the non-political character of the work must be understood by the people; they must have a real desire that it be done well; and they must make this the test by which they judge the person or persons responsible. In the opinion of the author the conditions in Washington are such that the establishment of a well organized administra-

tive system, headed perhaps by the State Board of Tax Commissioners, would be a great step in advance.

§4. Not only are the present arrangements unfavorable to the selection of the best man available, but when a good man is secured he cannot long be retained. The term for which the assessor is chosen is two years, and the constitution provides[4] that "No county officer shall be eligible to hold his office for more than two terms in succession." Under certain conditions such a provision has some justification. In so far as the work is merely supervisory a change, once in a while, helps to prevent the growth of abuses and the falling of the administrative machinery into a rut. Where, however, the work is that of a trained expert, long continuance in office should actually increase the value of the officer to the community; and where efficient service, rather than popularity, is the test by which a man is judged the danger that he will become intrenched in office is reduced to a minimum. In this connection, as in the selection of the assessor in the first place it is vitally important that the people shall really desire that the work be well done.

The difficulty created by the constitutional rule that the assessor shall be ineligible for more than two successive terms is sometimes partially overcome by electing a retiring assessor's chief deputy to succeed him. This would, at first sight, appear to be an important consideration since it would mean that the office would be filled by a man who had already worked in it for some years. It must be remembered, however, that the office in question is a political one, though it ought not to be; and it is greatly to be doubted whether the fact that a man has already served as chief deputy is a very great factor in securing his election. Indeed, in a large county comparatively few know who is the chief deputy; and in the campaign attention is largely centered on candidates for higher offices. It is probable, however, that the chief deputy has some advantage over his opponents. A few counties have secured the advantage of having experienced men by rotating the office between two, the one elected appointing the other as his chief deputy. Such a plan, however, can hardly be regarded as generally practicable.

The work of the assessor should be regarded as a profession for which a man will carefully prepare himself and in which he will look forward to a lifetime of service, subject to the possibility that he will be promoted to a higher office. This is, indeed, a con-

[4]Article XI, Section 7.

dition of attracting the best men to the work. Careful training is hardly worth a man's while unless there is some assurance that it will long be of use. Indeed it is probable that security of tenure is an important consideration to that type of mind necessary for the making of the expert. It is a question of the kind of ability as well as of the amount. We have, undoubtedly, some very good men among our tax assessors, but we should probably have more of them if the office were commonly filled by promotion or by the appointment of men trained elsewhere; and made vacant by promotion, death, disability, misconduct, or demonstrated incompetency.

§5. The pay of the assessor ranges from $4 a day in counties having a population of less than 16,000 to $2,200 a year in the largest. This seems small for a man who is required to ascertain the value of all taxable property in his county, from the lands and goods of an individual of modest means to the property of great corporations engaged in mercantile, manufacturing, or extractive industries. Some of the men with whom the assessor must deal are men of high ability, and however desirous they may be that the businesses which they represent shall deal justly with the state, are under strong inducements to keep taxes as low as possible.

It is hardly necessary, however, that the salary paid to the assessor be very large. In the first place, he is not an altogether independent official, but is subject to the supervision of the State Board of Tax Commissioners. In the second place, public office has attractions of its own, and the government can commonly secure, under favorable conditions, a higher grade of ability than can corporations for the same remuneration.

§6. The work of assessment is, of course, too great for one man to perform without assistance. Not only is there need of an office force, but a number of men must be appointed to share in the actual work of listing and valuing property. First of these is the chief deputy. The man with whom the ordinary property holder, at least in all but the smaller counties, comes in contact is a field deputy. In some cases experts have been employed for special lines of work, such as the "cruising" of timber lands, or the valuation of machinery or merchants' stocks in trade. In a few instances use has been made of appraisal companies, but cases of this sort are exceptional.

It is a constant source of complaint, on the part of assessors, that they are unable to secure competent field deputies. By a

state law the pay is limited to $8.50 a day; and in some cases the county commissioners have refused to allow even this much. It appears that in a few instances they have assumed the responsibility for allowing more. These men, it must be remembered, are engaged in inspecting property, in taking the declarations which the holders of personal property are required to make, and in agreeing with the owner as to the value of the property referred to in the declaration. Their work is, of course, supervised by the assessor, and is checked by data in his office, and of course the work of one field deputy can be used to some extent as a check on that of another dealing with similar property. If the taxpayer is not satisfied he may appeal to the assessor, but he is not likely to do so when the state would gain from the correction of an error.

As an illustration of the difficulty of securing competent field deputies the following may be quoted[5]:

"The next question to be considered is the selection of these men. Usually each one of the [County] Commissioners has some pet out of a job, likewise out of money. You are not in a position to turn these pets down, so you must place them on the list, regardless of what their experiences may have been. My experience has been that most of the good men you would like to have for the work are already employed and would not quit their present work for a job that would last only from forty to sixty days at three dollars per day. As a matter of fact we have to take such men as we can get for the work. Perhaps this year we shall have a larger field to draw from, as there are more unemployed men than usual. As it is I am short of applications for the work so far."

§7. While the county assessor is primarily responsible for the assessment of all property except the operating property of railroad and telegraph companies, his conclusions are not necessarily final, and he is subject to some control by the state authorities. His assessments may be revised by the county board of equalization and, as far as municipal taxes in cities of the first and second class are concerned, by the city board. The State Board of Equalization, while it does not change the assessments as equalized by the county boards, apportions the state tax on the basis of its own equalization.[6]

Among the duties of the State Board of Tax Commissioners is the supervision of the entire tax system of the state. So far as their other duties permit they are required to visit the various coun-

[5]S. C. Davis, Assessor of Lewis County, 16 Convention of County Assessors, p. 44.

[6]In regard to the methods of equalization see below, pp. 71-2 and 88-9.

ties, to confer with and advise the taxing officials, to be familiar with the methods adopted by them, to prescribe the forms and blanks that shall be used, and to determine what legal proceedings shall be taken. Their directions to the assessors and other officials are not merely advisory, but mandatory. In short, the law seems to contemplate a fairly thorough system of supervision. The commissioners, however, have no power to remove an assessor, though in cases of neglect or misconduct such as would, under the statutes, justify removal, they may set the law in motion. They have, of course, no power to choose assessors. The system is one of supervision, rather than of control.

§8. In this connection mention should be made of the annual convention of county assessors. Like a number of other county officials, including commissioners, auditors, and treasurers, the assessors have for a number of years been accustomed to meet annually to discuss the problems with which they are confronted in their work. Until a few years ago attendance at these conventions was voluntary, there being no provision in the law recognizing them. In 1911, however, the legislature passed a statute directing the commissioners to call the assessors together annually at Olympia for conference and instructions, and providing for the payment of the expenses of those in attendance.

The value of these conventions is very great. The author has had the pleasure of attending a number of them, and has been much impressed with the way in which the problems that have arisen in the different counties have been presented and discussed. Their proceedings[7] constitute a very important contribution to the literature of the subject, and should be available to all who are interested in the working of our tax system.

§9. While the work of assessment is necessarily extended over a considerable period of time, the law requires that all property where possible shall be assessed with reference to its value on the first day of March. The reasons for a definite assessment day require but little comment. Under the theory of the general property tax all property should be treated alike. Since the value of property is subject to some fluctuations, there would obviously be a chance of inequality if each person were taxed on the value of his property on the day upon which the assessor happened to call upon

[7]For some years printed without cost to the state by the Pioneer Bindery and Printing Company, of Tacoma.

him, and serious abuses would be possible. Nor is the particular date chosen a matter of indifference. The levy and collection of the tax require a considerable amount of time, and if taxes are to be laid according to the calendar year March 1st is a natural assessment day. Of more importance than this is the fact that the choice of the assessment day is not without its effect on the amount of taxes collected from different members of the community, since in some lines of business men are likely to have on hand a larger amount of personal property at some seasons than at others.

It has been suggested by one of the leading writers on taxation[8] that the very common selection of a day in the winter or spring is made in order to avoid placing much of a tax on the farmers' crops, these being usually specifically exempt in those States in which the assessment day is in the autumn. This, at first glance, may seem to result in an unfair discrimination in favor of the farmers. As a matter of fact, however, there seems little reason to doubt that the general property tax, in its actual working, bears more heavily upon the farmers than upon almost any other class in the community; and, in practice, assessment at a time when it will not fall upon crops in the hands of the farmers probably does more to remedy than to create an injustice. It would be much better, however, if the system were such that no remedy of this sort was necessary.

§10. Personal property in Washington is valued annually. Real property is valued only in the even numbered years, subject to readjustment in case property previously exempt becomes taxable, or in case improvements are made or removed. Except for such changes as these, taxes in the odd numbered years are based on the assessment of the preceding year. Annual valuation of personalty is in many cases practically necessary. The amount of such property held by any taxpayer is likely to change considerably from year to year; and even where the property is permanent in character changes in ownership are commonly impossible to follow. The case of real estate, however, is different. Changes in ownership may take place, but this does not cause any great difficulty since such changes can be followed readily, and, in any event, the tax constitutes a lien upon the property itself. The difficulty caused by changes in value is not so easily disposed of; but it may be questioned whether the hardship resulting is sufficiently great to warrant the expenditure that an annual

[8] C. C. Plehn, "Introduction to Public Finance," p. 265.

valuation would imply.[9] It is worth noticing that there are a few States in which valuation is much less frequent than it is in Washington.

§11. Prior to the legislative session of 1913 the law required that all property should be assessed at its true value in money, and specifically forbade the assessor to adopt any lower standard of value because it was to be used for the purpose of taxation. True value is so fully and carefully defined in the statute that any misunderstanding would seem to be impossible. Upon filing his books with the clerk of the county board of equalization (at that time the county auditor) the assessor was required to certify under oath that the value given for each kind and description of property was the "true and fair value" to the best of his knowledge and belief. In 1913 the law was amended so as to provide that property should be assessed at "not to exceed fifty per cent of its true and fair value in money."[10]

It is just possible that the law as it stood before this amendment was obeyed at some time in some county; but the author is unable to say when or where. Perhaps it has been obeyed in the case of a few individuals. As regards particular classes of property but one instance has come to the author's notice. "Other improved lands" in Skamania County were in 1908 assessed at one hundred per cent of their value, according to the findings of the State Board of Equalization. A careful search through unpublished records might reveal other instances. The Proceedings of the State Board of Equalization, as published by the State Board of Tax Commissioners, however, show no case in which all the property in any county has been assessed at its true value. Assessment at sixty per cent or more was unusual. The average for the State, previous to 1913, varied between 39.25 per cent and 43.96 per cent; and this in spite of resolutions, passed by the assessors in their annual conventions, that property should be assessed at sixty per cent of its true value. The amendment of the law does not appear to have had a very great effect on the practice; but in a few counties in the past two years the new law seems to have been observed.

§12. To many persons the requirement that the true value shall be used for the purpose of taxation seems useless if not pernicious.

[9]For a good discussion of the subject see Raper, "Frequency in Assessment," 8 National Tax Association, pp. 51-60.

[10]Remington and Ballinger Code III, Section 9112.

When a given amount of money is to be raised a high valuation means a low rate and a low valuation a high rate, the burden of taxation remaining the same. This is doubtless true so far as the same ratio of assessed to true value is used in all cases. As a matter of fact, however, the ratio varies greatly from county to county. In 1914, for example, the State Board of Equalization found that the ratio varied from 22.48 per cent in Klickitat County to 50 per cent in Clallam County, the average for the State being 42.30 per cent.

It is doubtless true that in so far as the State Board of Equalization is able to ascertain the ratio applied in each county[11] such discrepancies as these can be corrected, so that each will bear its fair share of the State tax. It is also true that if the assessors were required, in practice, to make use of the true value discrepancies would still exist, for different assessors would estimate true value differently. As will appear later, some difficulties of this sort seem to be inevitable under the general property tax. To allow the assessors any discretion as to the ratio, however, simply increases the difficulties of the State Board of Equalization, which are already sufficiently great. There can be no doubt that one important reason for assessment at a low ratio is often a desire to protect the county from an unfairly large share of the State tax. There is much reason to believe that the State Board of Equalization will not be successful in making the readjustment.

Even within the county assessment at less than true value is likely to result in inequality between individuals. As a matter of mathematics it is true that, other things being equal, a given rate on a fifty per cent valuation will have the same effect as half that rate on a hundred per cent valuation. Other things, however, are not equal, for as a matter of psychology, the attention of the taxpayer, at the time he deals with the assessor, is focused on the valuation, and he is less likely to insist that it be fair to him when he knows that the value for taxation will be considerably less than the true value. This, no doubt, makes matters easier for the assessor, and ease in assessment has been advanced as an argument in favor of a low valuation. If all taxpayers were equally affected the argument would be a good one, but as a matter of fact they are not all

[11]The figures of the board, as the best available, will be used frequently in the following discussion. They must, however, be received with caution. The Tax Commissioners themselves admit that accurate equalization is impossible and the railroad companies seem to feel very sure that it is not accomplished. See below, pp. 89ff.

equally affected. The low valuation will probably be found to have little influence on the man who has a considerable amount of property and is accustomed to dealings in values and percentages, and much more influence on others. Generally speaking, therefore, the effect would be to place an unduly large share of the burden on those least able to bear it.

It is sometimes argued that a low ratio of assessment tends to keep down taxes. This, too, is a matter of psychology. People have become accustomed to a high tax rate, and it is contended that were the valuation to be increased the rate would not be correspondingly reduced. Just as the taxpayer, in dealing with the assessor has his attention focused on the valuation, so the legislature and the other taxing authorities, in considering the amounts that may be raised by taxation, have their attention focused on the rate that contemplated expenditures will make necessary. Moreover, for the purpose of preventing excessive taxation, the statutes provide maximum limits for the rates that may be imposed; and these limits are presumably made on the assumption of a low valuation. Unless these statutes were changed an increase in valuation would, in effect, be the same as an increase in the maximum lawful rates.

There can be no doubt that the difficulty is both real and important. The attempt has been made to deal with it in some States that have recently made a real effort to secure the assessment at true value by statutory prohibitions of more than a moderate increase in the amounts to be collected in the near future or by a new statutory limit in the tax rate. In Ohio, for example, both methods have been adopted.[12] While there are some difficulties in connection with legislation of this sort, it would seem a necessary step in securing reform.

§18. It appears, however, that the chief reason for the recently imposed limitation on the ratio of assessed to true value was something different from the belief that a high valuation is a cause of high taxes. According to one proponent of the law[13] the only object was "to prevent excessive bonding." The right of the cities and counties to issue bonds is limited by the Constitution to a fixed

[12]See R. M. Ditty, "Uniform Rule and Tax Limit Legislation in Ohio," 6 National Tax Association, pp. 215-233. This paper is remarkable as being one of the very few presented before a body of tax experts in which an attempt is made to defend the taxation of all property at a uniform rate. The limit on the amounts that might be collected caused some difficulties and has been repealed. See comment of Commissioner Peckinpaugh, 8 National Tax Association (1914), p. 387.

[13]C. H. Shields, in "Taxation in Washington," p. 275.

per cent of the assessed value of the property within their jurisdictions. In some cases this limit has been very closely approached. Further borrowing can be made possible by an increase in the ratio of assessed to true value. It appears, therefore, according to this authority, that the reason for the limitation of assessed value was to restrict public borrowing.

Now, if it be admitted that there is any great danger of "excessive bonding" it is to be regretted that the danger could not be met by a frank and open amendment of the laws relating to public indebtedness. Doubtless there were in this case some serious difficulties in the way. A reduction in the nominal bond limit would have made necessary a readjustment in assessed values in many places. This would have given rise to much opposition, even if the object of the proponents of the law were generally approved. The indirect method was much simpler. A bill, however, the ostensible purpose of which is different from its real purpose will often receive some support to which it is not entitled, and it is not impossible that this is what happened in the present instance.

In favor of the existing law two things may be said: first, it recognizes the fact that property is not assessed at anything like its true value, and removes the almost irresistible pressure on the assessor to swear that he has assessed property at its true value, when he and every one else at all acquainted with the situation knows that he has not; and, second, it recognizes the serious difficulties in the way of reform. If we were to continue indefinitely to make use of the general property tax some effort should be made to overcome these difficulties. As things are it will probably be better to let reform in this matter wait upon a more thorough reform of the whole system.

Chapter V.

THE GENERAL PROPERTY TAX:

County Assessment; Valuation of Property

§1. While all property is supposed to be assessed at the same percentage of its value, different methods are used in the case of different kinds of property. This is as it should be, for the methods that may be found most satisfactory in one case may prove quite unworkable in another. Real estate, for example, is easily found, its ownership is a matter of record, and whatever may be the difficulties of ascertaining its value there would be little gained by applying to the owner for his estimate. For all kinds of personal property the law requires a declaration by the owner or some other person responsible for the property. In many cases the declaration is little more than a setting forth of the results of the assessor's own investigation. In others considerable reliance must be placed upon it. It is only in this way that some kinds of property can be found at all. Sometimes the property can be found but the value is so largely a matter of estimate that it is practically necessary to consult with the owner, and, if possible, come to some agreement with him. In other cases the value can be calculated, at least in part, but the calculation involves difficult problems in accounting. There are many kinds of property, both real and personal, and each class presents problems peculiarly its own. To attempt to deal with them all in the same way would be decidedly unfavorable to real equality in taxation.

§2. It is generally agreed that there are few, if any, classes of property that are more easily assessed than real estate. Land and buildings cannot hide and they cannot run away. In this State the assessor is required by law to "make out in the plat and description book in numerical order, a complete list of all lands or lots subject to taxation"; and in many counties the actual practice goes considerably beyond the minimum requirements of the law. Improvements can be, and commonly are, indicated on the plat. It is not difficult, as a rule, to determine whether or not a given piece of real estate is exempt. There is in this case nothing corresponding to the exemption of $300 worth of personalty to each head of a family.

But while real estate is readily found, it is not always easy

to determine its value. As a rule the difficulties are less serious than they are in the case of most kinds of personal property; but in some instances a valuation in which the assessor can have much confidence seems to be impossible. It might be supposed that in a community in which a large number of pieces of land are transferred every year something might be learned from the prices at which sales are made; but, as a matter of fact, the true consideration need not be expressed in the deed; and the instances in which it is not expressed are so numerous as to greatly impair the utility of this method. Experts on real estate values may be consulted, but their estimates are likely to differ widely.[1] It must be remembered that the State of Washington is developing rapidly; and this is naturally a cause of many changes and much uncertainty.

§3. In the case of urban land there is one consideration which generally outweighs all others in importance. This is location. To be sure, there are other things that must often be taken into account. The character of "local improvements," for example, makes some difference. Much of the land available for residences in our cities is itself unimproved, and the level of the lot may differ so greatly from that of the street that a considerable quantity of earth must be taken away or brought to it before a building can be erected. Such matters as these, however, are not the primary sources of difficulty.

The fact that in any city there are many real estate transactions makes assessment easier than it would otherwise be. It is true that little reliance can be placed on the consideration named in a deed; but frequent transfers do enable those familiar with them to form an idea as to the value of land in a given district. In many cases this idea is fairly accurate, and this is especially likely to be true when the land is divided into lots of uniform shape and size.

While maps and plats are commonly used, the methods of assessment are sometimes rather crude. The field deputy ascertains as well as he can the value of the different lots, and comparisons and corrections are made in the assessor's office. In recent years,

[1]The assessor of Yakima County secured estimates of the value of the land, exclusive of improvements, on which the Yakima Hotel stands. The highest estimate was $60,000; the lowest, $28,000. B. F. McCurdy, "The Basis and Equalization of Assessments," 14 County Assessors, p. 27. This may be an extreme case, but the experience of New York City in acquiring land for a court house is worth noticing. The following estimates, in round numbers, of the site are mentioned:

By a tax department deputy	$5,500,000
Experts for the city in condemnation proceedings	5,600,000
Experts for the owners in condemnation proceedings	9,500,000
Commissioners in condemnation	6,000,000

Lawson Purdy, 7 National Tax Association, p. 282.

however, the methods adopted have been made much more systematic. In some cases a good deal of reliance is placed on more or less mechanical methods. In this connection mention should be made of the Somers System,[2] although so far as the author is aware, it has never been fully used in any part of the State. An important feature of this system is the use of certain secret formulæ, and for this reason its application makes necessary the employment of a private appraisal company. Most of the fundamental principles on which it rests, however, are generally known, some of them having been in use before the system was devised, though discussion of the system has doubtless done much to popularize them. Some of these principles have been used by the assessors of this State.

In utilizing a system of this sort the first step is to prepare a map of the entire area to be assessed, the land being divided into blocks which are usually, though not necessarily, those made by the streets. A unit of measurement is then selected. In the Somers System this is a strip of land one hundred feet deep and having a frontage of one foot. The value of such a strip chosen from an inside lot in the block having the most valuable frontage in the city is then taken as a starting point and called 100, the value of similar strips elsewhere is then tentatively determined and expressed as a percentage of this. These tentative values are then presented for discussion by the public generally or by those best qualified to judge of land values. The theory is that while it is very difficult to secure agreement as to the relative value of given pieces of land, a consensus of opinion can be obtained as to the relative value of different frontages upon which considerable reliance can be placed.

Several problems still remain: the value of the most valuable frontage must be determined; allowance must be made for the varying depth of different lots; and the effect of the corner influence must be taken into account.

Since it is only in the case of the land having the most valuable frontage that the value must be determined directly, the problem is greatly simplified. In so far as the theory upon which the system rests is correct an error here will not result in inequality between different property owners within the district. This is, of course, of more importance than assessment at true value. Between different

[2]For a discussion of the Somers System from the point of view of an appraisal company making use of it see W. W. Pollock, "An Equitable Standard for Land Valuation," 7 National Tax Association, pp. 234-266. Mr. Pollock's address was followed by a discussion in which the system was severely criticised, pp. 267-285 and 449-454.

districts inequality may still exist; but there is no reason for supposing that it will be greater than would otherwise be the case. In fact it is likely to be somewhat less, since in the attempt at equalization attention can be largely focused on a comparatively small amount of land in each district.

Where the land is rectangular in shape and of standard depth, away from corner influence, the value of a given lot is readily obtained by multiplying the value of one strip by the frontage. For the purpose of dealing with lots of other shapes and depths the standard strip is divided into sections, which generally consist of one square foot. By the application of a rule based on accumulated experience the percentage of the value of the strip to be attributed to each section is then determined; and in the same way the value to be added for each additional foot of depth is determined. The fact that the rules applied for this purpose differ somewhat under different systems suggests that none of them is accurate. This is doubtless true; but it is still possible that nearer approach to accuracy can be secured with such a rule than with none. It would seem, however, that no one rule can be devised which will apply with equal accuracy under all conditions. It is probable, for example, that different rules should be applied in the case of business and of residence property.

The determination of the corner influence presents a difficult problem, and it is chiefly in this connection that the secret formulæ of the Somers System are supposed to be valuable. In general, it may be said that within a certain distance of the corner the value of each section of each strip is affected by two frontages, and these two influences must in some way be combined.

No doubt any mechanical system of this sort has its defects. The Somers System has been subjected to severe adverse criticism; but it seems to be generally admitted that some of the underlying principles are of considerable utility, though it is denied that they are peculiar to the Somers System. It must be remembered, moreover, that whatever may be the faults of a mechanical system, the alternative requires the exercise of judgment in a matter in which there is much difference of opinion, but no certain knowledge. To say just how far mechanical principles, such as those that have just been considered, are used by the county assessors of Washington would require a more minute study of actual methods than the author

has had the opportunity to make. It appears, however, that they are used in some of the largest counties.

Whether or not a mechanical system is used, the assessor is not, as a rule, entirely dependent on his own resources. In some cases substantial assistance is given by individual citizens or by associations that are in a good position to perform such services. In 1908, for example, the Seattle Real Estate Association, co-operating with the assessor, furnished an appraisal of land values in the city which has served as a basis for subsequent biennial assessments. The result according to Assessor A. E. Parish is "that substantial difficulties no longer attend the assessment of Seattle realty."[3]

The adoption of such a method as this implies, of course, that a considerable part of the work of assessment is done by persons not connected with the assessor's office. Under proper circumstances this is entirely legitimate.[4] So far, according to Mr. Parish, readjustments in the original appraisal have been readily made. It would seem, however, that ordinarily it would be necessary to call upon outside help at more or less frequent intervals. Possibly some system could be devised under which it would be possible to get help of this sort whenever needed, and to rely very largely on it.

§4. The problems with which the assessor must deal in determining the value of rural lands differ somewhat from those with which he is confronted in the cities and towns. Location is still of importance, but there are a number of other considerations which are either absent or of less significance under urban conditions. The character of the soil and the extent to which it has been cleared must receive a large share of his attention. Even the purpose for which the land is used is commonly taken into account, the value of the crop at the time the assessment is made being generally included as a part of the value of the land. Land planted with alfalfa, for example, may be assessed at $250 an acre, land in grain at $175, and pasture land at $125. The assessed value of orchard land is high because of the trees growing upon it.

As in the case of urban land, so in the case of rural, the methods of assessment are sometimes crude in character, and almost certainly

[3] "Administration of the General Property Tax," Taxation in Washington, p. 26.

[4] The Prussian Gewerbesteuer, or business tax, furnishes a good example of the systematic use of associations of taxpayers in the assessment of the tax. The system is worked out with true German thoroughness. For an account of it see J. A. Hill, "The Prussian Business Tax," Quarterly Journal of Economics, Vol. VIII, pp. 77 ff. This article is reproduced, in part, in C. J. Bullock's "Selected Readings in Public Finance," pp. 328-336.

very imperfect in results. The assessor of one such county states that it is practically impossible to ascertain the amount of land of a particular kind. "It is impossible for the deputy to go out and measure a field, or even approximate the acreage with any degree of accuracy, as there may be several fields, and in such irregular shapes that they are hard to even guess at the extent of them." As to valuation, the same assessor remarks, "about all the guide we have to go by is such sales as have been made, the price being usually hearsay." "As a matter of fact land values in this western part of the State are to a very great extent simply a matter of opinion."

In some of the counties, however, the attempt has been made to develop a scientific system of assessment.[5] For this purpose the land is divided into units, commonly of forty acres. Maps are prepared showing the ownership of all the farming land in the county, the character and quality of the soil, and any special advantages or disadvantages, such as roads and watercourses. The land is classified and graded, there being in some cases as many as ten different classes and as many grades. The systems used in the different counties are not uniform. From some points of view this is unfortunate; but it at least leaves the way open for experiment with different systems, and allows each county to adopt one specially suited to its needs or its willingness to bear the initial expense which the adoption of such a system implies. It would be well, however if a really scientific system could be worked out for the whole State. Possibly it might be so arranged that counties in which conditions are comparatively simple could adopt a part of the system at first, adding other features as they developed.

The initial cost of grading and classification has doubtless been one of the chief reasons why some system has not been more generally adopted. It must be remembered, however, that the cost appears to be somewhat greater than it really is, because it falls chiefly upon the year in which the system is first put into effect. According to the testimony of assessors of counties in which the work has been done, the cost of keeping the system up to date is small, as it is unnecessary to use a large number of deputies in the making of each biennial assessment.

[5] Yakima and Douglas Counties, for example, make use of systems of this sort. In Spokane County what appears to have been a very good system was put into effect by Assessor E. P. Galbraith, but, unfortunately its use seems to have been greatly impaired by the adoption of township assessment.

The question, however, is not merely one of cost. The great advantage lies in the relative accuracy and equality of assessment. Where no such system is adopted each parcel of land presents a difficult problem in itself, and where any attempt is made to compare different parcels it is comparatively easy to show that circumstances and conditions are substantially dissimilar. A system of classification and grading at least makes it possible to consider separately each of the different factors on which value depends, and thus goes far towards the simplification of the problem.

It is not, of course, to be expected that any such system can be entirely satisfactory, but there is little reason to doubt that it constitutes a great improvement on the haphazard method; and it is to be expected that with the accumulation of experience a nearer approach to perfection can be attained.

§5. In the assessment of permanent improvements, such as buildings, similar attempts at the establishment of a scientific system have been made. In some counties a card catalog is kept showing the character of all buildings within the county, or at least within a city.. Upon these cards may be entered such details as size, materials, mode of construction, date of erection, original cost, depreciation, and present value. Where such a system is adopted the amount of work necessary in connection with the biennial assessment is greatly reduced, since only changes need be noted.

The assessment of buildings presents, however, some serious difficulties that are either absent or of less importance in the case of land. It is doubtless an advantage that the original cost can be ascertained or the cost of production new estimated. Against this must be set the problem of depreciation. This is, of course, important in the case of certain kinds of land, but such cases are comparatively few, and depreciation is nearly always a big element in the case of a building. So far as what may be called structural depreciation is concerned, much may be accomplished by the use of established scales of depreciation, supplemented by observation. There are, however, many other influences bearing upon depreciation. Changes in the prevailing style of buildings, whether for business or for residential purposes, have a very material effect on value. The growth of a city may render a building unsuitable for the best use of the site on which it stands. It not infrequently happens that a building, still good from a structural point of view, is torn down to make way for a building better suited to the locality. In such a

case the building, no matter how good it might be if it were differently located, is worth no more than its salvage value.

Notwithstanding all difficulties, however, it is probable that, aside from land, there are very few forms of wealth that are easier to assess than are buildings. It would seem that it is possible, in many cases, to place the burden of proof as to special depreciation upon the owner, forcing him to accept the assessor's estimate or to present reliable evidence as to the amount of depreciation, even though that makes it necessary for him to bring forward facts that he would regard as too private a matter to be disclosed to the assessor in any ordinary discussion as to the value of his property.

§6. The system of careful surveys, followed by the maintenance of records that need only to be corrected to meet changed conditions has been more widely applied in the case of timber lands than in that of any other form of property. When the State Board of Tax Commissioners was organized in 1905 it found that the assessment of forests was largely a matter of guess-work. Since that time timber cruises have been made in practically all the timbered counties of the State.

The first of these cruises was completed in King County in 1908. Its character and effect are thus described by the assessor under whose direction it was made[6]:

"To determine the true value of timber and timber lands in King County * * * an official cruise was inaugurated in 1907 and completed in 1908, in which some twenty expert cruisers, with capable assistants, were employed under the general direction and supervision of one of the ablest timber cruisers of the West. Every timbered section in the county was carefully cruised, and detailed reports made upon each separate ten-acre tract, showing not only the kind, nature, quantity and quality of all timber and its accessibility for logging purposes, but the character and adaptability of the soil and the general topography of the county. These reports, as received from the field cruisers, were transcribed by office draughtsmen in India ink, photographed upon linen, bound in separate volumes by townships, and now form part of the permanent records of the assessor's office, from which absolutely correct assessments may be made for all future time, after due allowance for recorded logging operations.

"The cost of said cruise was slightly less than $70,000, and it resulted in an increased valuation of the timber lands of the county

[6]T. A. Parish, "Assessors and Assessments," 3 National Tax Association, pp. 335 and 336.

of over $12,000,000, and in additional revenue to the county therefrom, for the year 1907 alone, largely in excess of the expenditure for the entire cruise."

There is little reason to doubt that the effect of the timber cruises has been to make the law more effective, and to collect a large amount of revenue that would not otherwise have been obtained. Another result, however, has been to raise grave doubt as to the wisdom of the general property tax as applied to forests. Commissioner Rockwell, while admitting that the cruises have been of great value, says[7]: "We think we have come as nearly as possible to equality as can be expected under our present system, but the errors have been so glaring that it would be foolish for any one to argue that uniformity and equality have been obtained."

There are, however, other strong arguments against the application of the general property tax to forests, and these will be considered in their proper place.[8] Here it need only be noticed that those who advocate a change do not, as a rule, contend that the owners of the forests should pay less taxes than the holders of other forms of real estate of the same value. It is the method, rather than the amount of taxation to which objection is made.

§7. There is, perhaps, no form of real property more difficult to assess than mines. The mineral, to which the property owes its value, lies mostly under ground. The value of the mine depends not only upon the amount of mineral, but upon the rate at which it is taken out, the cost of the process, and the price at which it can be sold. As has already been pointed out, the price at which real property is bought or sold does not afford the assessor a sufficient indication of its value. In this case there is the additional difficulty that the value, as judged by this method, is largely speculative. Speculative value, while it might from one point of view be regarded as satisfying the letter of the law, does not furnish a good criterion of ability to pay taxes; and, in the opinion of the taxing officials, purely speculative value should not be considered.

In dealing with mines a distinction must be made between those that are operating and those that are not; and each of these may be divided into subclasses. It is claimed by some who are in a position to speak with authority that the value of the former can often be ascertained with a reasonable degree of accuracy. In some

[7] 4 Tax Commissioners, pp. 14 and 15.
[8] See below, p. 120.

States, as for example in Michigan, high grade engineering experts have been employed for the purpose. In Washington work is now being done on the classification of coal lands, which are the most important mineral properties in the State, somewhat along the lines adopted in the case of the timber cruises. Work of this sort is expensive if well done, but it will probably prove to be worth all it costs if the attempt to tax such property in the same way as other real property is continued.

In practice, under the conditions prevailing in the State, a great deal of reliance is placed upon data furnished by the operators of the mining properties concerned, supplemented by data secured from other sources. In some cases the operators seem to have co-operated with the assessors in a substantial way. One assessor testifies that they no longer fear to place their books, reports, and other more or less private information at his disposal. He then bases his estimate of value very largely on net smelter returns, though taking into account also offers or refusals of sale.[9]

When the operators co-operate in good faith with the assessors it would seem that the value of the property could be ascertained with a reasonable approach to accuracy. The success of the method is largely dependent, however, on the willingness of the taxpayers to give their assistance. Without in any way questioning the good faith of those who have already shown such willingness, it cannot be ignored that access to the books of the producers will not necessarily result in a fair valuation. Commissioners entrusted with the regulation of the rates charged by the public utilities have found how difficult it is, in the absence of prescribed methods of accounting, to ascertain the facts in regard to the properties over which they have supervision; and while the problems of the assessors may not be quite as great, they will probably be found serious enough to greatly impair the utility of this method.

The assessment of non-producing mines is even more difficult. Where they are associated with mines that are being operated, the valuation of the former may be based, to some extent, on that of the latter, though this can hardly be regarded as satisfactory. In some cases the assessment of non-producing mines is little, if any, better than guess-work. As the assessor last quoted remarks[10]: "We sometimes take a long shot with all the general and special information

[9] F. B. Wilson, 16 County Assessors, p. 52.
[10] Loc. cit., p. 53.

that we are able to get, taking care that the valuation placed is well within the limit. We seldom do this work arbitrarily if it is possible to confer with the owners or managers." The method adopted, as described by another assessor, is to "consult men who are fair and unprejudiced, considered competent and familiar with local conditions as well as the property in question."[11] How many such men he is able to find he does not say.

It is sometimes said by those interested in mineral properties that a mine that is producing nothing has no value for the purpose of taxation, and should be assessed only at the value of the surface land. This is, perhaps, an extreme view; but there are many who hold that the assessment of such property should be very low. It must be remembered, however, that the general property tax is not supposed to be a tax on income or on product. Under it property that has value should be taxed, regardless of whether it be productive property or not.

§8. It would, of course, be impossible to consider all kinds of real property in a work of this sort, or even to consider any of them fully. Some attention has now been given to those that are of greatest importance as regards the amount of revenue received and the extent of the interests affected. A few words may be added by way of summary.

Real estate is usually easy to find but the determination of its value is difficult. Complete accuracy is hardly to be expected, a remark which might be made of assessment under almost any form of taxation. With the aid of scientific methods much may be accomplished in the direction of securing a substantially just assessment. Such methods involve a considerable initial expense. Careful surveys must be made, and the results must be embodied in more or less elaborate records, which must be kept up to date. Property must be classified, and the factors that enter into the value of each class must be carefully considered. Substantial progress in this direction has already been made in Washington, but much remains to be done.

There are, however, certain forms of real estate in regard to which there is serious question as to the possibility of the successful application of the general property tax. Such is the case with mines and forests. As regards the latter there are other reasons than the difficulty of assessment for holding that special methods of

[11]LeRoy Marbelle, "Mine Taxation," 12 County Assessors, p. 20.

taxation should be used. Substantial justice in assessment, it must be remembered, does not necessarily imply substantial justice in taxation. Consideration of the underlying principles of the general property tax, however, is, for the present, postponed.

§9. Turning from real to personal property the difficulties of assessment are greatly increased. Personal property is of many kinds, some of which are very hard to find and some very difficult to value when found. That much personal property escapes taxation is generally admitted by the assessors themselves. Were they to deny it the statistics showing the results of the assessment would establish a strong presumption against them. In 1914, for example, the total assessed value of all property in the State, exclusive of the operating property of railroad and telegraph companies so far as these are assessed by the State Board of Tax Commissioners, as equalized by the county boards, was $898,842,448. Of this but $156,703,671, or about 17.4 per cent, was personalty.[12] No allowance is here made for exemptions, although it is possible that some property was ignored because it would have been exempt in any event. If only taxable property is considered, personalty constitutes about 14.3 per cent of the total.[13] Just what proportion of the property in the State is, in truth, personalty it is impossible to say, but even when allowance is made for the fact that most forms of "intangibles" are not property for the purpose of taxation it seems incredible that these figures can be correct.

§10. The statement that the assessment of personal property is a failure does not, of course, apply equally to all classes of such property. Live stock, for example, can generally be found and, upon the whole, is relatively easy to assess. In 1914 the total value of live stock, including poultry, as equalized by the county boards, was $20,239,665,[14] or about 12.9 per cent of the total personalty. The variation in average value between different counties, however, is remarkable. The average value of work horses, for example, varied from $22.62 in Klickitat County to $73.60 in Ferry County, the average for the State being $48.70.[15]

§11. A sort of property that has given the assessors a great deal of trouble is merchants' stock in trade. In 1914 the value of

[12]Computed from the figures given in the Proceedings of the State Board of Equalization, 1914, pp. 27 and 32.

[13]Loc. cit., p. 88.

[14]Loc. cit., pp. 14-18.

[15]Loc. cit., p. 15.

"goods and merchandise, including fixtures and appliances used in business," as equalized by the county boards, was $31,546,850,[16] or about 20.1 per cent of the total personalty. At one time a great deal of reliance seems to have been placed on the simple declarations of the taxpayers; but in some of the counties at least this has been abandoned. As T. A. Parish, a former assessor of King County, remarks, "for some inexplicable reason most merchants had acquired the habit, to which they clung most tenaciously, of returning valuations upon their stocks at the same amount at which they had been assessed in the preceding year, notwithstanding the fact that their business had increased and their stocks multiplied over and over again in value since the original assessment."[17]

Some of the assessors claim to have secured good results by sending out deputies especially familiar with the business they are employed to assess. It would seem strange, however, if a man, paid at the rate of $3.50 a day or less, could visit a store or warehouse and correctly estimate the value of the goods it contained. The method was tried in King County, but the results were not satisfactory. The taking of actual inventories by the deputies was, of course, out of the question. Finally, in 1908, the assessor asked the merchants to permit him to examine their books of records and accounts and their own inventories. As might be expected, this plan at first met with unanimous resistance; but finally most of the merchants consented. Upon the property of those who refused to make a full disclosure the assessor placed an arbitrary valuation sufficiently high to protect those who were co-operating with him; and the county board of equalization refused to grant relief unless the complaining merchants were able to prove substantial injury by submitting their records to the inspection of the full membership of the board.[18]

The same methods have been adopted in a number of other counties and seem to be regarded by the assessors using them as satisfactory. It must be remembered, however, as has already been suggested in connection with the use of similar methods in the valuation of mining property, that accounts may be kept in such a way as to fail to disclose the facts of the case. Indeed, the problem of the valuation of stock in trade is a complicated one, and different methods of accounting are commonly used by different concerns where

[16] Loc. cit., p. 24.
[17] "Assessors and Assessments," 3 National Tax Association, p. 338.
[18] Loc. cit.

there is no intent to deceive. In the absence of uniform methods of accounting it would seem that some inequalities must arise. It would be difficult, however, to find a method that is likely to produce a nearer approach to equality, especially if the figures are so presented that the assessor is able to analyze them.

Unfortunately, however, this method cannot be applied in all cases. To say nothing of the possibility of keeping accounts in such a way as to mislead the assessor, there are many concerns that fail to keep any adequate accounts, even for their own purposes; and these are sometimes concerns doing a considerable amount of business. In King County the attempt is made to deal with them by employing expert deputies, but the maximum payment of $8.50 a day has proved to be a severe handicap.[19]

There is another difficulty of a somewhat different sort. It is often possible for a merchant to allow his stock to become very low at the time of assessment. Canned salmon, for example, have ordinarily left the State by March 1st. An interesting exception occurred in 1908 when, partly on account of the industrial depression there was a considerable amount of canned salmon in the State at that time. The merchants tried to induce the assessor to pass them by, but he refused to do so.[20]

§12. Another form of personal property that has been a source of some difficulty is manufacturing plants. Here the most important item appearing in the published statistics is "manufacturers' tools, implements and machinery, including engines and boilers." In 1914 the total amount of property of this sort, as equalized by the county boards, was $11,555,963,[21] or about 7.4 per cent of the total personalty. Problems of much the same sort arise, of course, in connection with the machinery owned by other than manufacturing concerns.

Here, as in other cases, it is of course impracticable for the assessors to make much of an inspection of the property. In some cases they are able to make use of documents furnished by the manufacturers themselves. The owners of mills and factories, especially the larger ones, commonly have appraisals made for their own purposes; and these appraisals are sometimes used in determining the value of the property for purposes of taxation.

[19]A. E .Parish, "Equality and Uniformity of Assessments," 12 County Assessors, p. 40.

[20]T. A. Parish, "Assessors and Assessments," Loc. cit., p. 338.

[21]Proceedings of the State Board of Equalization, 1914, p. 24.

In other cases the amount of insurance carried is taken as a guide. This is regarded by some of the assessors as fairly reliable since the insurance companies will not permit over-insurance. There is, however, nothing to prevent under-insurance; and many business men fail to carry as much insurance as they might. If the amount of insurance carried is the best indication available to the assessors of the value of property of this sort, very serious questions might be raised as to the utility of other methods of assessment. Doubtless, however, the cases in which insurance is the only guide are comparatively few.

Apparently the method most commonly used is to base values upon cost. This introduces the very serious problem of depreciation; and in the opinion of the State Board of Tax Commissioners is likely to mean that the assessment is made by the officials of the company concerned. "The owner or manager," they say, "will be ready to show a great depreciation from first cost until, at the end of a few years, such properties are assessed at a very nominal figure, even though earning returns on a much higher valuation."[22]

Doubtless all of these methods may be combined and used together, but it will be seen that the assessor who can properly combine them must be an expert of a fairly high grade.

§13. The assessment of banks is fairly easy; but this is because the law itself makes unnecessary the listing and valuation of all personal property held by them. It is provided that they, or, more exactly, their shareholders, shall be taxed on the true value of their stock, less the assessed value of the real estate belonging to the bank. In the case of foreign banks the assessment is based on the "general average of money used as exhibited by daily or monthly balance sheets during the year preceding the time of rendering such tax lists to the assessor." A somewhat similar method is used in the assessment of building and loan associations. In 1914 the assessed value of the capital stock of incorporated banks was $12,884,572,[23] or about 8.2 per cent of the total personalty.

It will be noticed that while assessment is thus made comparatively simple, the method is radically different from that applied to other forms of personal property. Other corporations are not taxed simply on the value of their stock, either with or without a deduction of the assessed value of real estate. Nor is the result that

[22] 5 Tax Commissioners, p. 16.
[23] Proceedings of the State Board of Equalization (1914), p. 24.

the banks are taxed according to the value of their property, using the term "property" in the same sense as that in which it is used in other cases. In attempting to ascertain the value the assessors very commonly take simply the book value; that is, the sum of the capital, surplus, and undivided profits, and this method has the approval of the Tax Commissioners. Some of the assessors insist that true value means market value, and endeavor to make their assessments on that basis. Taking the law literally they are doubtless correct; but when the stock seldom comes on the market this method presents serious difficulties. Both methods represent a departure from the principles of the general property tax, particularly in a state in which stock is ordinarily exempt. Book value, however, represents the value of the capital owned by the bank and used in the business. Market value includes good will, which in the case of mercantile and manufacturing concerns is not assessed.

Special treatment of banks is not unusual in States making use of the general property tax, and is due in part, no doubt, to the regulations of the National Government in regard to the taxation of national banks. It does not follow, of course, that any injustice is done; and the banks do not, in general, seem to regard themselves as unfairly treated. In fact the general counsel of the American Bankers' Association classes the Washington method under the head of "other satisfactory systems," though he seems to prefer the New York method of a uniform tax on the book value of the stock.[24]

There is one feature of our law, however, which has been subjected to more or less adverse criticism. This is the deduction of the value of real estate from the value of the stock. It is obvious that it is to the advantage of the State that the banks own as little real estate as possible. In the case of some of the banks in Seattle, and presumably the same is true in other parts of the State, the value of real estate held exceeds the value of the stock; and, as a result no tax on the latter is collected.[25] It is argued that this gives an undue advantage to the stockholders of banks a large part of whose assets are in the form of real estate.

§14. The assessment of the most important of the public service corporations—railways and telegraphs—is, as far as operating property is concerned, in the hands of the State Board of Tax Com-

[24]Thomas B. Paton, "State Taxation of Banks," 7 National Tax Association, p. 319.

[25]A. E. Parish, "Administration of the General Property Tax," Taxation in Washington, p. 31.

missioners. There are, however, a considerable number of public service corporations whose property is within the jurisdiction of the county assessors. In 1914 the value of the "property of gas, electric light, power, water, telephone and other public service concerns, including franchises," as equalized by the county boards, was $15,085,665,[26] or about 9.6 per cent of the total personalty.

In the assessment of property of this sort considerable reliance is placed upon the declarations of the companies, though it can to some extent be checked by the investigations of the assessors and some light is thrown upon the subject by the data secured by the Public Service Commission. Valuation for rate making purposes and valuation for the purpose of taxation are two different things and are properly so regarded by the law.[27] Data collected for the former may, however, be of some service to the assessor in forming his own estimate of value.

The declarations which the public service companies are required to make are fairly elaborate, including a statement as to the amount and value of the stocks and bonds, and a detailed statement of the amount and value of physical property. The franchise itself is property for the purpose of taxation. Real, as well as personal, property must be listed. It may be noted, in this connection, that gas and water mains and pipes, laid in streets, roads, and alleys are classed as personal property.

The fact that the franchise is subject to taxation makes it less easy for the corporation to evade taxation on its personal property, since all value which the assessor believes to exist, but cannot definitely locate can be put under this head. It is sometimes said that the result is to tax the good-will of such companies, although this is not done in the case of corporations or individuals engaged in a private business.[28] While there is probably some foundation for this complaint, it should be noticed that good-will in the case of a public service company, if it can be regarded as existing at all, is ordinarily something different from the good-will of a private concern. Good-will seems to imply competition, whereas a public service corporation generally possesses monopoly powers.[29]

[26]Proceedings of the State Board of Equalization (1914), p. 26.

[27]See below, pp. 80-2.

[28]E. g., C. J. Hall (Tax Agent of the Pacific Telephone and Telegraph Company), "Valuation and Taxation of Telephone Property," Proceedings of the Sixteenth Annual Convention of County Assessors, p. 66.

[29]This matter is more fully treated in connection with the assessment of railroad and telegraph companies, p. 83.

Just how far the assessors are successful in determining the value of this class of property it is difficult to say. The companies themselves complain that they are required to pay more than their fair share of taxes; and it is probable that they are at least as fully assessed as are the owners of almost any other form of personal property. The publicity that necessarily attends their operations gives the assessor a material advantage. On the other hand, the valuation of property of this sort is a very difficult matter, as the public service commissions have found; and it would seem that it should be in the hands of a well paid expert. In some cases the difficulties are increased by the fact that there is no one assessing authority. An electric company, for example, may run a street car system and also sell electricity for light and power. The assessment of the street car property is in the hands of the State Board of Tax Commissioners; that of the light and power properties in the hands of the local assessor. Some of the public service companies operate in more than one county, and consequently no one assessor has full jurisdiction. It would seem, therefore, that there is in some cases a "twilight zone."

§15. There is one form of business property that should be mentioned, not because of its importance, the total value of such property in 1914, as found by the assessors and equalized by the county boards being only $888,359, but because it illustrates how information in the hands of the State is sometimes withheld from the assessors. Fish trap locations are property for the purpose of taxation. In order to hold such a location a permit must be secured from the State Fish Commissioner, and he has information in his office which would make the work of assessment relatively easy. This information he is forbidden under severe penalties to divulge, save for statistical purposes. The locations are known by the numbers on the licenses, and even if no more were done than to use the same numbers for the same locations year after year it would be a help to the assessors. The numbers, however, are changed every year, presumably for the convenience of the commissioner in keeping his books.

§16. In the assessment of many kinds of personal property the assessor must rely almost entirely on the taxpayer's declaration, supplemented by his own judgment. This is true of some kinds of business property. It is even more generally true of property used for the comfort and convenience of the owner and his family. In

many cases the deputy assessor visits the taxpayer's residence, though he sometimes goes to his place of business. It should be sufficiently obvious that any careful inspection by the deputy is out of the question. Even if a complete list of the property were obtained in this way it would be of doubtful utility, for there is still the serious problem of valuation. The deputy can hardly be an expert judge of the value of the thousand and one things that are to be found in the home of a well to do citizen.

It is probably true that outright dishonesty on the part of the taxpayer is not as common as is often supposed. The assessors themselves say that only a small proportion wilfully make a false statement. It is often difficult, however, for the taxpayer to give a complete list of his property, especially when he is not stimulated thereto by self interest. Regular inventories are not as common in the home as they are in the office. Commonly he has only a very general idea of the value of the various articles. He knows that if he were to attempt to sell them he would get comparatively little for them, for they would have to be sold at second hand. He knows, too, that values for the purpose of taxation are commonly low; and though he may be willing to pay his fair share of taxes he does not want to pay more. In practice he is likely to place a large part of the burden of making the estimate on the deputy. If the latter names an amount which he regards as in reason he will often approve it. In some cases—probably in more than is generally realized—he will say that the value named is too low. The deputy, however, is naturally unwilling to take an unfair advantage of the man who is trying to do his full duty, by placing upon his property a higher valuation than would be placed on that of the man who takes a less public spirited attitude. His estimate, therefore, is likely to be conservative.

There can, however, be no doubt that many taxpayers try to keep the assessment at as low a point as possible. Often they will name an amount that will bring their property safely within the $300 exemption; and some of the assessors believe, on this account, that the law granting the exemption should be repealed. Upon the whole, there is probably no exaggeration in the statement that the taxation of household goods "has always been farcical in the extreme."[80]

If the difficulty were merely that a considerable amount of property of this sort escapes taxation the situation would not be as

[80] 4 Tax Commissioners, p. 10.

bad as it is. There is much to be said in favor of the exemption of such property. To say nothing of the effect of evasion on public morals, the fact is that all property owners are not equally affected. Here, as usual, it is likely to be the small property owner that suffers most. His goods are relatively few in number and are of the kind most familiar to the deputy. It is much more difficult to assess valuable pictures, rugs, and similar household articles.

§17. While a full discussion of the assessment of personal property is impossible in a work of this sort, enough has been said to give some idea of the way in which the assessors work and the problems with which they are confronted. Experience has shown that assessment is not a simple matter of receiving the sworn declarations of taxpayers. Where reliance must be placed mainly on the declaration the tax is generally a failure and a bad one. In practice more than the declaration has been found to be necessary. In some cases "expert" deputies must be employed. In others books and papers must be examined. In the case of some corporations, particularly the public utilities, assessment is, in reality, based largely on earning power, this being taken as the main guide to the value of the property. All these difficulties suggest that, at least as far as personalty is concerned, the general property tax fails to accomplish its purpose.

In any event it should be recognized that the assessment of both real and personal property is a difficult matter, requiring trained ability as well as integrity on the part of the assessor. If the taxation of many kinds of property is to be continued the work of assessment should be better organized; and organized for the State as a whole. The office of assessor should be taken out of politics and made attractive to men with a professional spirit and professional training.

§18. The work of the assessor is, of course, subject to correction by the county and city boards of equalization. The county board is composed of the county commissioners, the county treasurer, and the assessor. In cities of the first and second classes three councilmen are selected who, with the county commissioners, constitute the board of equalization for property within the corporate limits. These boards have the right to revise the assessment of any parcel of land, of any class of personal property, or of the property of any individual. No increase, however, is valid unless due notice is given to the taxpayer. Persons who feel that they have been unfairly treated

have a right to appear before the board, or to file complaint in writing.

While a considerable number of changes are made by these boards of equalization, it is hardly to be expected that they can do much to bring about real equality in taxation. Only a comparatively small portion of the property assessed receives special attention, and this chiefly in cases where complaint has been filed. Generally speaking, the other members of the board are not in as good a position as is the assessor to know the real value of any particular piece of property. Where evidence is presented to them that has not been presented to the assessor they can make corrections, and in a few cases they can doubtless discover serious errors affecting classes of property. All this, however, is something substantially different from bringing about uniformity in assessments.

It does not follow that the boards of equalization are useless. The power lodged in the assessor is so great that some opportunity for appeal and for review is desirable. Appeals might, of course, be considered by the courts in the first instance, but their methods of procedure are not the best for the purpose, and the use of boards of equalization seems simpler and more convenient. The courts can, of course, act only when complaint is brought before them. It is well for the assessor to know that the results of his work will come under the review of a board specially organized for that purpose, and that special attention may be called to details by anyone that is dissatisfied, without the formality of court action or the necessity of presenting the sort of evidence that a court requires.

A taxpayer who thinks that he has been unfairly treated by the assessor and the board of equalization, may, of course, bring the matter before the courts, but he should be very sure of his ground before he does so. The courts are very slow to interfere with the valuation of property for the purpose of taxation. Ordinarily they are inclined to regard the action of the board of equalization as final unless fraud or malice can be shown.[81]

As has already been pointed out, the state board of equalization is not concerned with the assessment of individual taxpayers, except in the case of railroads and telegraph companies, which are assessed by the Tax Commissioners instead of by the local assessors.

[81] "In no case has this court ever interfered with an assessment of property for purposes of taxation upon the sole ground of excessive assessment, in the absence of a showing of actual fraud on the part of the assessing officers, where the difference between the assessed value and the actual value was as small as ten per cent."—N. P. Ry. Co. v. The State of Washington, 84 Wash. 510-544.

Chapter VI.

THE GENERAL PROPERTY TAX:

State Assessment.

§1. The operating property of railroad and telegraph companies is assessed by the State Board of Tax Commissioners. The terms used in the law assigning them this function are broadly defined. As railroad companies are classed all persons, associations, and corporations operating railroad stations, terminals, or bridges, and those operating street or interurban railways as well as those operating the long distance lines. As telegraph companies are classed those owning or operating cable or telegraph lines and engaged in performing telegraph service for compensation. Telephone lines and wireless telegraph stations, however, are not included. In all cases it is the operating, rather than the owning company with which the Commissioners deal.

It must not be inferred that state assessment implies any separation of the sources of state and local revenue. Taxes on the operating property of railroad and telegraph companies are collected in the same manner as are taxes on other kinds of property, save only that all the property of street railway companies and telegraph companies is regarded as personalty. The same rates are imposed and the proceeds are divided between the State and its subdivisions in the same way. The Commissioners simply determine the value of the property within the State and apportion it to each county on the basis of mileage. The results are considered and, if necessary, corrected by the State Board of Equalization. The value assigned to each county is then reduced so as to make the ratio of taxable to true value conform to that which is found by the State Board of Equalization to be used by the county authorities in the case of property locally assessed. From this point on taxes on the property of railroad and telegraph companies are treated in the same way as are taxes on property of other kinds.

§2. The chief reasons for state assessment are to be found in the peculiar nature of the property and its relation to the locality in which it lies. A railroad or telegraph company does not ordinarily confine its business to a single county. To be sure the track and structures of a railroad company and most of the physical property

are definitely located in one county or another; but these are properly regarded as parts of a single property rather than as individual properties in themselves. The larger property includes some elements which have no definite location, such, for example, as the franchise. The application of the "unit rule," or the assessment of the property as a whole, prevents the escape of these elements. If the attempt were made to split up the property into its parts and to assess each separately some of them would be very likely to be overlooked or underestimated, with the result that the sum of the parts found would be less than the whole.

In the case of railroads there is the additional difficulty that much of the physical property can easily be moved from one place to another. If it were taxed in the county in which it happened to be on assessment day it is very likely that, if found in the State at all, it would be found, so far as was practicable from the point of view of the company, in those counties in which the taxes were lowest, either because of a low tax rate or because of a low valuation. The different counties would therefore have a strong inducement to bid for the presence of such property on March 1st by making the assessment as low as possible. It seems that in the days when assessment was in the hands of the local officials there was a very considerable difference in the valuation per mile of line in the different counties, and in all it was very low.[1]

There is at least one other objection to local assessment. The valuation of the great public utilities presents many difficult problems. The local authorities cannot as readily secure the data necessary for an accurate assessment as can a state board, and were they to secure it many of them would be unable to make a proper use of it. Not only this, but the necessity of dealing with a large number of local assessors would place a heavy burden upon the companies concerned which, in all probability would be shifted in one way or another to the persons making use of their services. All these difficulties are much less serious when the matter is handled by a state board, assuming, of course, reasonable success in the selection of its members.

The different reasons for state assessment do not apply with equal force in all cases. Telegraph companies have no rolling stock. In other respects, however, the advantage of the application of the "unit rule" is very much the same as in the case of railroad companies. Street railways, with some important exceptions, have all

[1]See 1 Tax Commissioners (1906), p. 89.

their property, both tangible and intangible, located in a single county. Many of the difficult problems of assessment, however, remain. Since the State Board has the responsibility for the assessment of other forms of railroad property, and has experience in the work it seems reasonable and wise to treat street railway property as other railway property is treated.

There are, then, four main reasons for state assessment: even so far as individual elements of the property are definitely located they are but parts of a larger whole which can be most accurately assessed when treated as a unit; much of the property, particularly the franchise, has no definite location; some of it may readily be moved on assessment day to the counties that will make the best bids for it; and the difficulties in collecting and utilizing the necessary data can best be met by a state board.

§3. Since the steam railway and telegraph systems are generally interstate, rather than merely intercounty, properties it may seem that the arguments for a central assessing authority point to the desirability of a federal rather than a state board. From a purely fiscal point of view the case for federal assessment is a strong one. The wider range of the National Government in the selection of officials and the greater dignity attaching to federal office should make it possible to secure a higher degree of ability for the work. This, together with the fact that a federal board would have substantially the whole of the railway and telegraph systems under its supervision, might be expected to result in a more accurate assessment. Even if it be conceded that the state boards are successful in their valuations they must necessarily duplicate each other's work to a greater or lesser extent, and this implies additional expense, part of which falls directly upon the people of the states and part of it indirectly since so far as it falls upon the companies it may be expected to be shifted eventually, meanwhile resting on the companies. A federal board could, moreover, adopt some definite system for apportioning the value to the different states, thus avoiding a certain amount of injustice which naturally results from the attempt on the part of each state to attribute to itself as much of the value as its sense of justice or the power of the courts will permit.

The objections to federal assessment are chiefly, though not altogether, political in character. Considering its exclusive authority over interstate commerce, it would probably be constitutional for the National Government to take into its own hands the determina-

tion of the value of most of the railroad and telegraph property, and the apportionment of this value among the states. The problem, however, is one of state rather than of federal finance, and the states are rather jealous of their rights. Even though the constitutionality of federal assessment be conceded, it is probably, for the present, politically impracticable.

While the advantages of federal over state assessment are similar in character to the advantages of state over county assessment there is a considerable difference in degree. A State, such as Washington, can afford to employ men of considerable ability. While the state board does not have under its supervision any of the interstate systems in their entirety it does have a considerable part of them. Much of the data that is needed from outside of the State for the application of the "unit rule" can be obtained without great difficulty. While there is undoubtedly a considerable amount of duplication of work where each state makes use of the "unit rule" it is not intolerable, as it assuredly would be if the attempt were made by each county; and a certain amount of duplication is not wholly without compensation, since the work of one board can be used to check that of another.

It should be noticed, moreover, that the State is greatly aided by the activities of the National Government. Railroad and telegraph companies doing an interstate business are subject to the jurisdiction of the Interstate Commerce Commission, which not only prescribes their methods of accounting, but makes available for the public a large mass of information of other kinds. If this Commission did nothing else the publicity that it assures would be of great value. Moreover the Commission is now making a physical valuation of the railroads; and while the importance of this may easily be exaggerated, especially with reference to value for the purpose of taxation, it may be of some help.

§4. It is only the operating property of railroad and telegraph companies that is subject to state assessment. Property owned by them but used for other purposes is still subject to the county assessors. Real estate, for example, which is held simply for investment must be reported to the commissioners but they are not directly concerned with its assessment. Telephone and telegraph property, though owned and operated by the same company, are assessed by different authorities. So, too, when an electric company operates

a line of street railways and at the same time furnishes electricity for light, heat and power, it is only the railway property that is assessed by the commissioners.

While there are some things that are clearly operating property and some that are not, there are others in regard to which a decision is difficult. Since it is desirable that a uniform policy be followed and since the State Board of Tax Commissioners has supervision of the entire tax system, the determination of the matter is naturally left to it. The matter may be brought before it as the result of a dispute beween a corporation and a county assessor, or the company may itself ask for a classification. A hearing is then held and evidence presented, or the members of the Board may make a personal inspection of the property. If it appears that the property in question is necessary to and used in the operation of the system, a finding to that effect is made; and this debars the county assessor from placing the property upon his rolls.

As illustration of the sort of questions that may arise may be taken the case of a warehouse.[2] If it were owned by a railroad company and used in connection with its freight business it would pretty clearly be operating property. The Commissioners find, however, that such property is frequently leased to private individuals at a nominal rental, the amount being only sufficient to show a valuable consideration for the lease. In this case the warehouse is still regarded as operating property. Again, grain warehouses are often built by private companies upon the right of way on land leased from the railroad at a nominal rental. Here the warehouse is assessed to the warehouse company and the land to the railroad, the latter being included in the operating property. Sometimes stock yards are erected upon land owned by the railroad adjacent to its track, the railroad looking for its remuneration to the business thus brought to its lines. Here the Commissioners take into consideration all the facts and circumstances that they regard as pertinent and make their decision accordingly.

The definition of operating property is a matter of some consequence, both to the corporation and to the counties concerned. Operating property is assessed without regard to county lines, and its value is then distributed on a basis of mileage. As a result the value of such property as terminals and warehouses is spread over the various counties in which the railroad has its right of way. This

[2]This, and the examples immediately following were kindly furnished the author by the State Board of Tax Commissioners.

is, of course, unfavorable to such counties as King, Spokane, and Pierce, in which the large cities, and consequently the most facilities of this sort, are situated. If such property were locally assessed it would help to swell the valuation of the county and municipality and thus make possible a lower tax rate. As it is, a part of the value is regarded as lying in the smaller counties. This is, of course, favorable to them, and since the tax rates for all purposes are smaller there than in the counties containing the large cities, it is favorable to the corporations whose property is thus assessed.

It is clearly desirable that all property used in the operation of a railroad or telegraph system should be assessed as a unit. It does not follow, of course, that distribution of the value on a strict basis of mileage is desirable; and the merits of the complaints of the larger counties can best be considered in connection with the apportionment of the value among the counties.

§5. The powers of the State Board of Tax Commissioners for making an assessment seem to be ample. An elaborate declaration is required of each of the companies concerned. Witnesses may be summoned and examined under oath. Upon notice to the company depositions of witnesses outside of the State may be required. The Commissioners may personally examine the property. The Public Service Commission[3] has made its own valuation of many of the properties concerned and has collected a considerable amount of information of which the Tax Commissioners may make use. The reports of the Interstate Commerce Commission are, of course, available. The corporations concerned have a right to a hearing at the time the assessment is made, and most of the large railroad companies take advantage of this right.

The law prescribes in some detail the character of the declarations that the companies are required to make, providing nineteen questions for railway and twenty-two for telegraph companies, and giving to the Commissioners the power to add others. As a result each of the declarations makes a considerable volume. Besides various facts as to their history, organization, and officers, railroad companies must give full information as to the amount, nature, par, and market value of securities; the amount of interest and dividends paid thereon for a series of years; securities of other companies owned by or held in trust for the company making the declaration; details as to mileage, considering the mileage of each kind of track

[3]Strictly the regulating body was the Railroad Commission until 1911, but to avoid cumbering the text the present name will be used in this discussion.

in each city, town, school, and road district in which the company operates in the State; income and its disposition for a series of years; rolling stock; taxes paid in other States; a description of all lands except those held under the land grants, whether used for operating purposes or not; and several other items. They must also file copies of their reports to stockholders, to the Interstate Commerce Commission, and to the public utility commissions of this and other States in which they operate. The declarations of street railway and telegraph companies are similar in character. These declarations must all be made under oath by the president or other chief officer and of the secretary, treasurer, auditor, or superintendent.

In case of failure on the part of the company to make the declaration or to furnish the information required of it the commissioners are required to make the assessment as best they can, and the company must accept their conclusions unless it is prepared to show that substantial injustice has been done. As a matter of fact the Commissioners have no trouble in securing the reports required.

As we have seen in connection with county assessment the declaration is often an unreliable method of determining the value of property or even the facts on which a correct estimate can be based. This, however, does not apply to the property of railroad and telegraph companies to anything like the extent to which it does in many other cases. Railroads and telegraphs are managed by public service companies and are subject to regulation both by the National Government and by the states in which they operate. Except so far as they lie within a single state even their methods of accounting are prescribed by the Interstate Commerce Commission.

As regards most of these properties it must be remembered that Washington is one of the states in which a complete valuation has been made for the purpose of regulation. This is not true of all the properties, but it is true of the most important of them. A value that is fair, both to the State and the corporations, for regulation is not necessarily fair for taxation; and the Tax Commissioners are not bound to accept the findings of the Public Service Commission.

§6. To many it seems absurd that there should be two distinct values for the same thing; and the Tax Commissioners have not always had the power they now possess. The two commissions were established by the same legislature. Apparently each had the right to make its own valuation, but the Court held[4] that the power of

[4]State ex rel. Oregon Railway & Navigation Co. v. Clausen, 63 Wash. 535.

the Tax Commissioners to make an independent valuation was confined to those cases in which the Railroad Commission had not acted. In 1911, when the Public Service Commission was established to take the place of the Railroad Commission it was provided that its valuation should furnish a minimum below which the Tax Commissioners might not go. On the assumption that there can be only one value this provision seems illogical. In 1913 it was repealed, and the Tax Commissioners now make an independent valuation when it seems proper to them to do so. Soon after this change was made there was an unsuccessful attempt made to deprive the Tax Commissioners of their power by initiative legislation.

The reasons for independent valuations by the two commissions can best be understood if it is kept clearly in mind that the Public Service Commission is concerned with the value on which the companies should be allowed to earn, if they can do so by fair methods, a fair return. For them the amount of the legitimate investment, on its cost side, is a consideration of primary importance. The Tax Commissioners are concerned with the actual value of the property as a business proposition. This is dependent primarily, not upon cost, but upon net earnings. The distinction is fairly well brought out if it is said, without any attempt to speak with scientific accuracy, that the regulating authority is concerned with the value that ought to be; whereas the taxing authority is concerned with the value that is. These two values are not necessarily the same.

It may be thought that the Public Service Commission should so regulate rates that the "true" value, dependent as it is upon earnings, would conform to its "fair" value. This, however, is not always practicable. To consider fully why it is not would require a study of the very complicated problems connected with the establishment of "fair" value and "fair" return. Such a study would here be out of place, but a few of the important points may be noticed.

First of all, the authority of the Public Service Commission is confined to the State of Washington. Even if it were successful in determining accurately the value of the property within the State it would have no power to regulate the rates on interstate traffic, nor could it use its power on business done entirely within the State to offset what it regarded as undue profits on interstate traffic. In so far as the regulations imposed by the National Government are

more or less favorable to the companies than those imposed by the state the "true" value will be greater or smaller than the "fair" value as found by the Public Service Commission.

In the second place, quite apart from any conflict of national and state authority, the power to fix rates is subject to limitations imposed by economic conditions. It sometimes happens that, owing to an original mistake in entering a given territory or to a change in conditions, there is no possible rate that will enable the corporation to earn a fair return on its legitimate investment. In such a case the "true" value will necessarily be less than the "fair" value.

Finally, to consider only one other point, commissions have commonly found that the rate situation in a given territory must often be considered as a whole. If, for example, there are two competing railroads the rates that one is able to charge are limited by the rates charged by the other. If the rates permitted to both are such as to allow a fair return on the more expensive road the "true" value of the other will be higher than the "fair" value that might otherwise be found to exist. If the cheaper road be limited to rates that will yield it only a fair return the other, even if permitted by the commission, cannot collect higher rates, and its true value will be less than its "fair" value. Often it is found that both justice to the company having the more expensive property and public welfare require that both roads should be allowed to exist and earn some profit. With the question of what policy the regulating authority should adopt we are not here concerned. Whatever be their policy the "true" value of at least one of the roads will differ from its "fair" value; and this will be the case as long as by "fair" value is meant the value on which the company should be allowed to earn a fair return, and by "true" value the amount that the property is actually worth.

A practical illustration is furnished by the Oregon-Washington Railroad and Navigation Company. The Tax Commissioners found that this road, running from the wheat fields of Washington to Portland, Ore., by what is largely a water level grade, was constructed at low cost. The value placed upon it by the Railroad Commission was very much less than its market value as determined by the capitalization of its earning power. The Interstate Commerce Commission could not reduce its rates without very injuriously affecting other railroads.[5] In this case the "true" value was considerably more than the "fair" value.

[5]Former Commissioner Frost, "Taxation in Washington," p. 142.

There is then nothing absurd or unreasonable in the use of two distinct valuations. The term "value" is not used in the same sense in both cases; and regulations based on the supposition that it is are very likely to result in injustice. It is entirely legitimate, however, for each of the commissions to make use of the data collected by the other; and, as a matter of fact, the Tax Commissioners have relied to a considerable extent on the facts found of the Public Service Commission.

§7. The first assessment by the Tax Commissioners was made in 1908. At that time four of the railroads, including the Northern Pacific and the Great Northern, had just been valued by the Railroad Commission; and the findings made and the values fixed by that body were taken by the Tax Commissioners as the basis of assessment.[6] In general they seem to have made use of similar findings wherever practicable, exercising their own judgment since they have been at liberty to do so, in readjusting the valuation so as to make it more appropriate for the purpose in hand, or in the making of corrections that they regard as desirable.

Since so much reliance is placed on the findings of the Public Service Commission an examination of its methods would be interesting and not without importance. Such an examination, however, is quite out of the question in this place. In general, it may be said that its investigations have been detailed and elaborate. In the case of the Northern Pacific, for example, the records were examined to show original cost of construction; engineers were employed to examine the property in detail, so far as it lay within the State, to determine cost of reproduction, depreciation, and present condition; the market value of the securities over a period of years was ascertained; statistics showing density and character of the traffic were collected. On the basis of all the information obtained the value of the property within the State was determined.

In some cases, especially where findings of the Public Service Commission were not available, the Tax Commissioners made use of what is known as the "stock and bond" method. By this method valuation is based chiefly on the market value of the stocks and bonds, averaged over a period of years. Since the securities, taken together, represent ownership, their value may be regarded as the market's estimate of the value of the property including intangible

[6] Tax Commissioners (1908), p. 19.

as well as tangible elements of value. While much may be said in favor of this method, especially if the term "market value" be taken strictly, it should be noticed that the estimate of the security market is affected by a number of considerations that have little bearing on the fundamental value of the property. The policy of a corporation as to the distribution of profits as dividends or their investment in the business, for example, has an effect on current quotations. Special conditions may cause securities to be put on the market at a sacrifice. In some cases at least the Commissioners have adopted the plan of "checking" the value thus obtained by the capitalization of net earnings at a rate equal to the ratio of average dividends to the market value of the stock.

In some instances the stock of a corporation practically never appears on the market, and consequently no quotations are available. Such was the case, for example, with the Oregon-Washington Railroad and Navigation Company, substantially all of whose stock was held in the interest of the Union Pacific. In this case the Tax Commissioners placed upon the property a valuation based upon the capitalization of net earnings at a rate which, in the judgment of the Commissioners, would have to be paid for money on similar security.[7]

The objection is made by the corporations assessed by the Tax Commissioners, as it is by the public utility companies locally assessed, that the methods adopted are such as to include "good-will," or "going concern value," whereas this is not done in other cases. There is some ground for this objection, notwithstanding the fact that "good will," in the case of natural monopolies does not mean precisely what it means in the case of competitive concerns. If the idea of taxing property is to be adhered to strictly, earnings that are due to the superior administration of property should not be capitalized in determining taxable value. Any special privilege, however, such as that represented by the franchise is property, and if it has value should be taxed. If value as a going concern is to be regarded as property, as in many cases it is, it should be taxed in all cases. The best excuse for the different treatment of public utility companies is that the extra value is primarily a franchise value, and that it is impossible to distinguish between its primary and its secondary character.[8]

[7]Former Commissioner Frost, "Taxation in Washington," pp. 142-3.

[8]In a very recent decision the Supreme Court distinguishes between good will as an intangible value due to the personal element and good will as an intangible value attaching to the property regardless of ownership. Northern Pacific Railway Company v. the State of Washington, 84 Wash. 510-544.

§8. Whatever be the methods adopted for determining the value of an entire system, the problem necessarily arises as to what portion of it should be attributed to the state. The taxation of property used in interstate commerce is, of course, subject to limitations imposed by the National Government; and a considerable number of decisions bearing on the subject have been made by the courts. In the light of these decisions there seems to be no doubt as to the constitutionality of a tax that is, in good faith, a tax on property, or even upon earnings, within the State; and which embodies neither a discrimination against interstate commerce nor an attempted regulation of it.[9]

In determining the proportion of the value of property used in interstate commerce that should be apportioned to the State, as in determining the entire valuation, much is left to the discretion of the Commissioners. The Board is directed[10] to take into account the mileage of the entire system and of that portion of it which lies within the State "together with such other information, facts and circumstances as will enable the board to make a substantially just and correct determination." The last clause is of great importance, since Washington is a state in which valuable terminal properties are located and in which a large amount of interstate business is done.

As a matter of fact the Tax Commissioners rely very largely on the findings of the Public Service Commission. It must be remembered that this body has made an elaborate and detailed study of the railroad and telegraph systems, and for the Tax Commissioners to duplicate their investigations would involve considerable expense. Here again, a study of the methods adopted by the Public Service Commission would be interesting, but is impracticable. Again, however, a few points connected with the valuation of the Northern Pacific may be noticed. So detailed was this investigation that on the basis of several of the tests used much of the property that should be attributed to the State was definitely located there. Where an apportionment was necessary various methods were used, depending upon the particular element of value under consideration. Generally, but not always, it was some form of mileage, such as passenger mileage, engine mileage, etc. Bringing the various elements

[9]For a general discussion of the subject see Seligman, "Essays in Taxation" (8th edition), pp. 264-270.

[10]"Shall' in the case of railroads, "may" in the case of telegraphs. Otherwise the provisions governing the two are substantially identical.

of value together, and combining them in a manner that cannot be clearly seen in the findings, the total value of the property within the State was determined.

The value of the rail and telegraph property within the State having once been fixed and due allowance made for "commercial," as opposed to operating, property, the annual assessment consists simply in making such adjustments as changes in conditions or new information seems to warrant. Here again reference is made to the findings of the Public Service Commission. The earnings of the companies as shown by their annual reports are taken into account. A very important consideration, in the opinion of the Tax Commissioners, is the location of a railroad and its connection with the transcontinental lines, special attention being paid to the character of the district through which it runs with reference to its ability to furnish a large amount of traffic.

§9. The value of the operating property within the State is apportioned among the counties on a mileage basis. In the case of telegraph companies single wire mileage is used. In the case of railroad companies the track is classified as main line and branches, and each of these is subclassified as main track, second track, etc., and sidings. Branches are assigned a value per mile equal to a percentage of the value of the main line. This percentage is not the same in all cases, but depends on earning capacity, as ascertained by the Commissioners. The values of the Palouse and Grays Harbor branches, of the Northern Pacific, for example, which run through good territory, were in 1914 fixed at forty per cent of the main line value per mile, the other branches bearing thirty-five per cent. Second track and sidings are treated in a similar manner, sidings being commonly, though not invariably, regarded as worth, per mile, twenty per cent of the value of the main track with which they connect.

It will be noticed that the method of apportioning the value of operating property to the counties differs considerably from that of determining how much of the value of the system lies within the State. For the State the different elements of value were separately considered and, wherever possible, each element that could properly be regarded as located within the State was definitely assigned to it. The value of terminal properties, for example, at least as far as it was dependent on cost, was not prorated over the system. Where an apportionment was necessary it was based on whatever principle seemed most appropriate—cost of construction, ton mile-

age, car mileage, etc. In the case of the counties, however, attention is confined to track mileage, modified only by the classification of trackage. The value of terminals and similar properties is therefore prorated over the counties in which the company has its lines. For this treatment of the counties the Tax Commissioners are not, of course, responsible. They simply act in the manner required by law.

As has already been pointed out this arrangement is not satisfactory to the counties in which such property as the terminals is located. Just what policy should be followed is a matter on which students of taxation are not in entire agreement. It is understood, of course, that mileage, as a basis of apportionment, is not exact, but is adopted as a practical measure designed to work substantial justice. The question is whether or not it is even approximately fair.

§10. The argument in favor of the present system is fairly simple. Operating property should be valued as a unit. It is only as a part of a railroad system that a terminal has value. Each county through which the road runs contributes to its traffic, and so to its earnings. While it is true that the terminals are physically located in the large cities, their value depends on the earnings of the system. To give to the terminal counties all the taxes secured from such property would be, in effect, to permit them to tax the business provided by the rest of the State.

From one point of view the argument for track mileage, if it be accepted at all, proves too much. It is not only the counties in which the railroads lie that supply traffic and thus contribute to earnings. It would seem that those that have no railroads at all should have some share of the taxes. The case becomes very much stronger when consideration is given to the smaller political divisions, such as the school districts. That a system that excludes them is unfair is the opinion of some students of the subject.[11]

While something may, perhaps, be conceded to the view that traffic is an important consideration, especially when this is applied to the business as a whole, and not simply to terminal property, it must be remembered that the tax is not supposed to be upon traffic or earnings, but on property. Real property is almost universally taxed

[11]See Brindley, "Discussion of Assessment of Railroads," VI National Tax Association, p. 503.

The Washington State Board of Tax Commissioners includes in its "List of Indictments against the General Property Tax" that it is "A system that distributes the revenue from public service corporations only to such counties and minor taxing districts as are fortunate enough to contain wire or rail mileage." 5 Tax Commissioners, p. 20.

where it lies, and if personal property is taxed otherwise it is ordinarily taxed at the domicile of the owner—a principle which in this case can have no application. It should be noticed also that the argument here applied to terminals might, on the same ground, be applied to jobbing houses, factories, and, still more, to docks and warehouses that are not operated as a part of a railroad system. While property might, in spite of custom and precedent, be regarded as constructively in the place from which business is derived, it would be better to do away completely with property as a basis for taxation. Another plan would be to separate the sources of state and local revenue, assigning all taxes from property of this sort to the State. Either of these plans would require a constitutional amendment.

§11. If, however, the larger counties wish to secure a change in the law so that the value of terminal property will be assigned to them they must urge something stronger than the desirability of strict adherence to the theory of a property tax and of the consistent treatment of different kinds of property. It is not difficult to see that there is much to be said for the justice of their position.

It is no accident that the terminals are located in the larger communities. It is there that the large commercial and industrial enterprises on which the terminal business is dependent are to be found. It is there that provision is made for the labor that is employed. So close is the relation between the terminal and the city that if the former were established and successfully operated where no city existed one would grow up around it. Not only does the city offer advantages as a terminal point, but the presence of the terminal implies large public expenses that must be defrayed by taxation.

Very much the same argument may be applied, though with somewhat less force, to freight and passenger stations, warehouses, elevators, etc., along the line. Their location is not ordinarily arbitrary or accidental. They are established at the points which offer the best facilities; and they ordinarily bring with them expenses that must be defrayed by taxation. There are doubtless exceptional cases. If it were possible it would be well to deal with each case on its merits. Except so far, however, as discretion is vested in the apportioning authority, the law must be framed with a view to normal conditions.

In the case of other forms of operating property the practical advantages of the mileage basis are greater and the argument that

it results in substantial injustice is much weaker. Doubtless, in view of the work of the Public Service Commission, it would be possible to apply to the local taxing districts the same methods that are applied to the State as a whole. This, however, would involve some expense, it would give rise to political difficulties, and it may be seriously questioned whether it is necessary in the interest of justice.

The investment of a large amount of wealth in the form of track, bridges, tunnels, etc., in a given county is ordinarily due, not so much to the advantages to be found there as to the physical difficulties of the country. While the presence of a railroad doubtless adds something to the expenses of the county or city through which it passes, in much the same way as does the presence of a terminal, there would seem to be a reasonably close relation between the mileage and the extent to which it does so.

Upon the whole the difficulties of apportionment strongly suggest the desirability, in the case of properties of this sort, of some form of taxation other than the general property tax. If, however, this tax is to be continued it would seem that mileage, with some allowance for terminals and similar property, is about as satisfactory a method as is available.

§12. The assessed value of the operating property of railroad and telegraph companies is not, of course, finally determined until it has been acted upon by the State Board of Equalization. As regards property of this sort the work of the Board may be divided into two parts: it has to determine how far the Commissioners have succeeded in ascertaining the true value; and it has to apply to the value apportioned to each county the ratio of assessed to true value applied by that county to other forms of property.

Until the legislative session of 1915 the State Board of Equalization consisted of the State Auditor, the Commissioner of Public Lands, and the State Board of Tax Commissioners. At that session an attempt to abolish the State Board of Tax Commissioners was defeated only by the Governor's veto. As a preliminary to the abolition of the Board a bill was passed, over the Governor's veto, providing that the place of the Commissioners on the Board should be taken by a member of the Public Service Commission to be designated by the Governor.

The change in the personnel of the Board will, perhaps, result in some changes in the methods by which it does its work. The part played by the Tax Comissioners, however, has been so impor-

tant that some consideration may well be given to the methods heretofore adopted. Moreover, if the Tax Commissioners are to remain a permanent part of the taxing machinery of the State it is not impossible that they will be restored to their places on the Board of Equalization.

In its attempts to ascertain how far the Tax Commissioners have been successful in ascertaining the true value of the property assessed by them the work of the State Board of Equalization is very similar to that of the county boards. The State Board may increase or decrease the valuation fixed by the Commissioners, and in the former case must serve due notice on the corporation concerned. Interested parties may, of course, appear before the Board and the more important public service corporations commonly send their representatives.

In connection with this phase of the work there is perhaps some excuse for the removal of the Commissioners from membership. Heretofore they have constituted a majority of the Board, and consequently the assessments that they have previously made could not be changed without the consent of at least one of them. If the Board of Equalization is to be regarded as a tribunal to which appeals can be taken it would seem that they should not be under the control of the board making the original assessment.

Quite different is the case as far as the determination of the ratio of assessed to true value in the counties and its application to railroad and telegraph property is concerned. The collection of data for this purpose has heretofore been done very largely by the Commissioners. It is difficult to see how any of the present members of the Board of Equalization are in even approximately as good a position to do this work as are the Commissioners. It is possible that the latter will continue to collect the data, though it seems to be more properly the work of equalization.

In order to ascertain the ratio of assessed to true value in the counties the Commissioners have heretofore spent a considerable part of the summer, in the even numbered years, in traveling over the State and taking sworn testimony in each county as to the actual consideration in real estate transfers. Lists were made showing values based on this testimony and the values found by the assessors. At its regular session, which is held in September, the Board of Equalization considered the information thus collected, and received further testimony from public service corporations, from assessors,

and from other interested parties. On the basis of all the facts before it the Board formed its opinion as to the ratio applied in each county.

§13. Just how far the system of state assessment has been successful in securing the fair valuation of the operating property of railroad and telegraph companies it is impossible to say. Not only would the answer to such a question involve a knowledge of what the property is actually worth, but it would involve a knowledge of the extent to which the State Board of Equalization is successful in ascertaining the ratio of assessed to true value in the counties. There are, however, some reasons for thinking that as a result of state assessment the corporations in question pay at least their full share of taxes.

There can be no doubt that under this system the valuation of the railroads has been enormously increased. In 1907, the last year in which such property was locally assessed, the total assessed valuation was $43,603,546. The next year it was $84,642,349, or something less than twice as much. After that it increased rapidly till 1912 when it was placed at $135,522,077. It fell off, for the first time, in 1913 but fell only slightly. In 1914 it was $137,538,331.[12] This is an increase in valuation in seven years of nearly 211 per cent. During this time the number of miles of line increased from 3,806.62 to 5,246.81,[13] or about 38 per cent.

Taking into account only the period during which assessment has been in the hands of the Commissioners, the increase in valuation was a little more than 62 per cent, while the valuation of all other property in the State increased a little less than 34 per cent,[14] and the mileage of line about 25 per cent.

In its report for 1912, the Board of Tax Commissioners, in calling attention to the great increase in valuation that had taken place, said that "today the steam and electric railroads operating in the State of Washington are assessed higher and pay a greater amount of taxes, measured by any known or accepted standard, than in any other state in the United States.[15] This hardly seems credible, but if true it affords a very strong presumption that the railroads were

[12]For the valuation in each year see Fifth Biennial Report, State Board of Tax Commissioners, p. 38.

[13]Statistical Abstract of the United States. The later figures do not include switching and terminal companies.

[14]Computed from figures in Fifth Biennial Report of the State Board of Tax Commissioners, p. 39.

[15]Tax Commissioners, p. 7.

unfairly treated. Taking the figures per mile of *line,* which is hardly a fair test, for the year ending June 30, 1913, which presumably covers the taxes of 1912, the railroads paid to the State of Washington $769 per mile. This was exceeded in New Jersey, Rhode Island, Massachusetts, the District of Columbia, New York, Connecticut, Ohio, and Pennsylvania, in the order named.[16] Considering what these exceptions are, they do not greatly weaken the conclusion that the railroads have just ground for complaint.

Looking at the matter from the point of view of percentage of taxes to earnings, the figures are rather startling. For four of the five largest systems of the State the figures are as follows:[17]

	Gross Earnings in Washington.	Net Earnings in Washington.	Taxes.	% Taxes to gross Earnings.	% Taxes to net Earnings.
G. N. Ry.	$ 9,480,504	$2,379,044	$ 932,450	9.84	39.20
N. P. Ry.	17,304,341	5,613,748	1,711,367	9.89	30.48
C., M. & St. P. Ry.	4,263,095	619,628	461,722	10.83	74.51
S., P. & S. Ry.	3,632,004	1,836,753	440,174	12.12	23.97

These figures certainly seem very high, even when allowance is made for the fact that the last few years have been rather unfavorable for railroad earnings.

The mere fact that taxes are high is not, of course, conclusive evidence that the railroads are not fairly treated. The railroads are supposed to be taxed at the same rate as are other forms of property, and complaints of high taxes are very common. A strict application of the general property tax would in many other cases result in the practical confiscation of the profits on which the value of the property is dependent. It is contended, however, that the ratio of assessed to true value is really very much higher in the case of the railroads than it is in the case of other forms of property. This means that the State Board of Equalization is not successful in ascertaining the ratio applied in the counties. Notwithstanding the efforts of the Board, and especially of the Tax Commissioners, it seems possible that there is some truth in the complaint. The Tax Commissioners themselves, in their "List of Indictments against the General Property Tax," declare that it is "a system that does not permit of equalization either between individuals, corporations, or

[16]Statistical Abstract of the United States, 1914, p. 280. The fact that the taxes of terminal and switching companies are not included in these figures strengthens rather than weakens the complaint of the railroads.

[17]Figures in the first three columns were furnished by the State Board of Tax Commissioners. The accounts of the Washington-Oregon Railroad and Navigation Company are kept in such a way that it is impossible to make a similar comparison.

communities."[15] It is safe to say that this indictment is supported by the views of the vast majority of students of taxation in America.

Assuming that the complaints of the railroads are well founded, the fault lies primarily in the nature of the system. The law does contemplate the taxation of property of this sort at a higher rate than other property is taxed. Many forms of property either cannot be found, or, if found, cannot be correctly valued. The value of the property of railroad and telegraph companies is subject to investigation by two state commissions that devote a considerable portion of their time to the work. While the property is complex the valuation depends on investigations much more elaborate and searching than are made in most other cases. The corporations owning it are relatively few in number and are regarded by many as "special interests," less willing than ordinary taxpayers to bear their share of the public burdens, or at least more able to escape. They are in the spotlight, and any concessions made to them are likely to evoke public criticism. The Board of Tax Commissioners has had to fight for its life at every session of the Legislature since it was organized. It would be but natural if the Commissioners were inclined to decide in favor of "the public" all doubts that arose.

The true interest of the public is, of course, justice, rather than the collection of undue amounts from any one set of taxpayers. It is true that so far as shifting of taxes takes place injustices of this sort are at least partially remedied. It must be remembered, however, that railroad rates are subject to regulation, and even when shifting takes place, the process is likely to be slow and expensive, and that eventually the costs of shifting, as well as the taxes shifted, are borne by the public. In the meantime much injury may be done to innocent parties.

Upon the whole the author is inclined to believe that, while political considerations may possibly have led to the imposition of undue tax burdens on the great public utility corporations, the main reason for excessive taxation, if taxation is really excessive, is to be found in the fact that the general property tax is more effectively applied to this form of property than to most other forms. The remedy is to be found, not in a reversion to the old, ineffective methods, but in a change in the system. If this is at present impracticable efforts should be made to extend efficiency in assessment to as many forms of property as possible, meanwhile making

[15] 5 Tax Commissioners, p. 20.

such corrections as are possible through the boards of equalization. If this fails, as fail it almost certainly will, to secure justice in taxation the need for a change in the system will be all the more clearly demonstrated.

§14. If the taxation of property is to be continued it is desirable that the whole system of assessment be more highly centralized. Even if this is not done there are certain classes of property the assessment of which by the Commissioners is especially desirable. This is true of the property of public utility companies of practically all sorts. It is also true of registered watercraft.

Attention has already been called to the source of the chief difficulties in the assessment of public utility properties by the county assessors. In the first place, it not infrequently happens that the same corporation operates property subject to State and property subject to local assessment. A street railway company, for example, may sell electricity for other purposes, all the power being derived from the same plant. The franchise, which is property, covers all purposes. In the second place, property, though subject exclusively to local assessment, may lie in more than one county. Telephone properties may be cited as an example. "The local and long distance business is so intermingled and mixed up that assessors have repeatedly protested that a correct valuation, as between counties, or even locally, is impossible."[19] In the third place, the Commissioners, with their close relation with the Public Service Commission and their greater familiarity with the work, are in a much better position to make the assessment.

That a change of this sort should be made is recognized by the assessors. In their report for 1910 the Tax Commissioners recommended a bill providing that the assessment of light, water, heat, and power properties should be placed in their hands. The following January the assessors, in their annual convention, passed a resolution that the assessment of all public utilities should be given over to the Commissioners. The bill, however, failed of passage. In 1912 the Commissioners recommended a new bill, this time including telephones. At the next convention of the assessors this bill was endorsed. Like the former bill it failed of passage.

The reasons for state assessment of registered water craft are very similar to those for the state assessment of railroad rolling stock. The proper *situs* for such property is very difficult to determine. As

[19]Fourth Biennial Report, State Board of Tax Commissioners, p. 18.

a result it is very likely to be found in the county that offers it the lowest valuation. "In many instances the value put upon vessels by the local assessor does not reach 10 per cent of the true value."[20] As in the case of public utilities other than railroads and telegraphs, legislation to provide for state assessment has been twice recommended by the Commissioners, twice approved by the assessors, and has twice failed of passage.

§15. Upon the whole, state assessment as carried out in Washington seems to be clearly justified in theory and in practice, if the more effective application of the general property tax to certain classes of property can be regarded as a justification. If anything can be said against this it is, so far as the available evidence goes, that it has in some cases led to excessive valuation. While, however, it is impossible to speak with confidence, it is the opinion of the author that the injustices that have arisen are due not so much to valuation that is, in itself, excessive as to the singling out of certain forms of property for effective treatment.

It would, of course, be impossible to treat all classes of property as the operating property of railroads and telegraphs has been treated. Not only would the task be far too great for the Commissioners themselves to handle, but there are classes of property that cannot be effectively reached by any known method. What has been accomplished in the case of the railroad and telegraph companies has been possible only because of the work of two state commissions, one of them working by very elaborate and expensive methods. There are some forms of property to which similar methods could be applied. There are many to which they could not. Doubtless something could be accomplished by a better organization of the assessing machinery; but this is not enough.

The experience of Washington seems to support the view, almost unanimously held by students of taxation, that the general property tax cannot be so applied as to work justice.

[20]Fifth Biennial Report, State Board of Tax Commissioners, p. 31.

Chapter VII.

BUSINESS AND CORPORATION TAXES

§1. For the taxation of corporations and of business Washington relies mainly on the general property tax. There is no general corporation tax save a moderate franchise tax on joint stock corporations and on a few other kinds. There are, however, a few lines of business, most of which are ordinarily carried on by corporations, that are subject to special forms of taxation. Express and private car companies pay a tax on their gross receipts and insurance companies a tax on their premiums. There are a number of license payments, some of which may be regarded as taxes, and the rest as fees.[1] In addition to these there are, of course, a large number of fees paid on special occasions, such as the filing of articles of incorporation, the taking of examinations for admission to the practice of certain professions, inspections, etc. With fees, as distinguished from taxes, we are not here concerned. We shall therefore leave out of account payments that are primarily fees and ordinarily regarded as such, merely calling attention to a few cases in which they seem decidedly excessive from that point of view.

Even when this is done consideration must be given to number of payments with which the State Board of Tax Commissioners has little or nothing to do, although the law creating that body specifically gives it the power and duty of exercising "general supervision of the system of taxation throughout the State." The franchise tax on corporations in most cases, and automobile licenses are in the hands of the Secretary of State; the Insurance Commissioner is responsible for the assessment and collection of the special taxes on insurance; local officials formerly had charge of liquor licenses in the counties and municipalities, although a portion of the proceeds were paid to the State. The Tax Commissioners, however, administer the privilege taxes on express and private car companies and until recently attended to the enforcement of the state liquor license taxes.

§2. Before considering the franchise tax on corporations it should be noticed that the "fees" paid to the Secretary of State so far exceed the expenses of the office that they should be regarded as containing a considerable measure of taxation. For the biennium

[1]For the distinction between fees and taxes see above, p. 4.

ending September 30, 1914,[2] the total expenses of the office were $25,501.68. During the same period "fees" for the filing and recording of articles of incorporation alone were $82,539.65; fees for the issue of certified copies amounted to $5,845.10; and for the reinstatement of stricken corporations $4,560.00. In addition to these candidates for political office paid $6,667.00. It will be seen that leaving out of account automobile licenses, which should be regarded in part as fees, and the franchise tax, the office was run at a profit of $74,164.07.

While, however, these corporation fees must be regarded as containing a considerable element of taxation, the total amount received is not very great. Judged by ordinary standards the charges made would hardly be regarded as specially exorbitant. The highest is $25 for the filing of ordinary articles of incorporation, regardless of the amount of capital involved. There are a few classes of corporations for which the fee is somewhat smaller. Included in the total are a number of fees, such as those for the appointment of agents, which are not itemized in the reports.

§3. The annual franchise, or corporation license, tax is but $15 a year in each case. With the exception of a few classes specially treated, such as insurance companies, it is imposed on all corporations having joint stock and on some classes of corporations not organized for profit. It is, of course, in addition to all other taxes, which in the case of most corporations means simply the general property tax. It is exclusively a state tax, none of the revenue being distributed to the localities. For the biennium ending September 30, 1914, the receipts for corporation licenses amounted to $297,290.[3]

The methods of assessing and collecting this tax are quite simple. No notice or tax bill is sent, but the corporations are expected to make payment when it becomes due. Failure to do so renders them liable to a penalty of $2.50 a year for the first two years. The Tax Commissioners have authority to start suit to collect the tax. Failure to pay is regarded as *prima facie* evidence of insolvency; and the corporation has no power to start or maintain a suit before the courts. At the end of two years its name is stricken from the list kept in the office of the Secretary of State. Upon proper application the corporation may be reenstated, but it must

[2]Figures are taken from the Thirteenth Biennial Report of the Secretary of State (1914), p. 10.

[3]Loc. cit.

pay the back taxes, fees, and penalties and, in addition, a penalty of $20 a year for the time during which it was stricken.

A corporation tax of $15 a year seems very moderate. Unless, however, it is desired to place special burdens on the corporate form of business activity any tax of this sort, under the conditions existing in Washington, must be small. Under the State constitution the property of corporations must be taxed in the same way as is other property. In so far as the ordinary corporate franchise actually confers an advantage it furnishes tax paying ability. While the certificate of incorporation might, in such cases, be regarded as property and taxed as such it is not ordinarily done. It will be noticed, however, that in the case of properties valued under the "unit rule" there is comparatively little chance for property of this sort to escape. Even in the case of manufacturing and mercantile corporations it seems probable that other forms of property are more readily found and taxed than in the case of private individuals and firms doing an equal amount of business. Upon the whole, however, when the moderate rate of the franchise tax and the difficulty of reaching the value represented by incorporation are considered, the tax can hardly be regarded as imposing a serious burden.

§4. Turning now to the special corporation taxes, attention may first be given to those imposed on insurance companies. Strictly this is not a corporation tax, since the term "company" is so broadly defined as to include individuals, partnerships, and unincorporated associations as well as corporations. As regards the amount and manner of taxation some distinctions are made, but these do not turn on the fact of incorporation. In particular, fraternal insurance is exempt from most of the fees and taxes that must be paid in other cases.

Before considering in detail the taxes imposed there is one qualification that should be noted. The insurance code contains a "reciprocal," or more properly a retaliatory, provision.[4] Where any other state imposes upon the insurance companies of this State greater obligations or prohibitions than Washington imposes upon foreign insurance companies the regulations of that state must be applied to its own companies.

Insurance corporations are subject to incorporation expenses similar to those imposed in other cases. These fees, however, are in nearly all cases paid to the Insurance Commissioner instead of to

[4]Insurance Code, Section 47.

the Secretary of State. In general, insurance companies must pay a fee of $20 for the filing of their annual statements of condition and report of business done in Washington. Fraternal benefit insurance companies, however, are exempt from this fee as they are from all taxes, fees, and licenses for which the insurance code provides, save only an annual license fee of $10. Such societies as the Masons, Odd Fellows, etc., are completely exempt. Title insurance companies are required to deposit certain securities with the State Treasurer as a guarantee fund, and to pay a fee of one-tenth of one per cent of the value of such securities. There are a few other fees of somewhat less importance.

Instead of the annual franchise tax insurance companies pay an annual fee of $10 for a certificate of authority to do business in the State. In addition to this there are a considerable number of licenses. There is an annual license fee of $2 on agents and solicitors, collected from each company that they represent. In the case of non-resident special agents the fee is $5. For insurance adjusters it is $10, but an agent of a duly authorized company may do the work of an adjuster without payment of this fee. "Non-admitted" companies are, under certain circumstances, allowed to do business in the State, but in such cases the agent must pay a license fee of $100 and make the annual reports on which the premiums tax is based. A license fee of $100 is also collected from insurance brokers. The license fee for non-resident special agents and that on adjusters are new, being authorized by the legislature of 1915.

Leaving out of account the fee for a certificate of authority, which is very much like the franchise tax paid by other corporations, and the annual licenses, the fees received by the Insurance Department are far from sufficient to cover expenses. In 1914 these fees amounted to $6,721.35[5] The expenses were $25,461.80. Even if the fees for the annual certificates of authority be included the result is not greatly affected, as they amounted to only $3,817.00. If these and the annual license fees be included, however, the amount is $52,886.35. It would seem, therefore, that even if all of these items are to be regarded as primarily fees they contain a considerable element of taxation.

When the taxation of insurance is mentioned what is commonly had in mind is the tax on gross premiums. This does not, of course,

[5]All figures here used are taken or computed from the Tenth Biennial Report of the Insurance Department (1915), pp. 12-13.

apply to fraternal insurance societies, nor does it apply to title insurance companies, since the law provides that the latter "shall be taxed on a basis of physical property * * * in the county where such property is located in accordance with the general laws relating to taxation in this state, and not otherwise."[6]

In all other cases there is a tax of two and a quarter per cent on all premiums collected or contracted for. Previous to 1915, however, this tax, in the case of life insurance companies, was only two per cent. Life insurance companies now receive less favorable treatment than do those engaged in other forms of insurance, since in computing gross premiums they are allowed to deduct only the amounts paid as premiums to "admitted" companies for reinsurance, whereas others are allowed to deduct these and the amounts paid to policy holders as returned premiums. In all cases the tax is reduced to one per cent if the company has as much as fifty per cent of its assets invested in bonds or warrants of the State or its subdivisions, in taxable property within the State, or in first mortgages upon improved real estate within the State. This provision, however, would not seem to be of great importance in the case of insurance companies doing business all over the country.

No difficulty is experienced in connection with the collection of the tax. Ordinarily the companies themselves calculate the amount and send in a cheque with their annual reports. In some cases, however, they wait for the verification of the report before making payment. The law provides, however, that in case of failure to make the report or to pay the tax within thirty days of the time specified, the corporation shall be subject to a fine of $25 for each additional day of delinquency. The tax may be collected by distraint; and the Insurance Commissioner may revoke the certificate of authority until taxes and fines are fully paid.

The tax on gross premiums yields a considerable revenue. In 1914 the life insurance companies paid $148,635.02; the fire insurance $133,061.78; miscellaneous, $36,784.40; and "unauthorized" companies, $2,833.86; making a total of $321,315.06.

§5. The singling out of any particular class of business for special taxation, where the purpose is really taxation and not regulation or restriction, may be justified on one of two main grounds: either the business cannot be as effectively reached by the ordinary methods as can other lines, or it represents a special measure of

[6]Insurance Code, Section 204.

tax paying ability. Where any class of business involves special activity on the part of the state, it may be legitimately required to make payments for the defraying of these expenses; but such payments are at least somewhat in the nature of fees. Those who condemn the taxation of insurance—and they are very many—commonly admit the legitimacy of fees that are only sufficient to cover the cost of supervision. Taxes in Washington are far in excess of this amount.

If it be desirable to tax insurance as heavily as other lines of business representing as much wealth are taxed, it must be admitted that the general property tax is in their case a particularly bad failure. Though possessed of enormous assets there is comparatively little that the property tax can reach. Their investments are largely in forms that are exempt in this State; and if they were not exempt it would be difficult to say just how much of the assets should be regarded as within the jurisdiction of the State. Unless, therefore, special forms of taxation were adopted it would seem that the insurance companies, notwithstanding their great wealth and the large amount of business done, would pay very little in the way of taxes.

It will hardly be contended that the insurance companies represent any special measure of tax paying ability. On the contrary, lack of ability is commonly urged as a reason for exemption or at least for great lenience. Here a distinction must be made. When the business is carried on by a joint stock company, organized for profit, there would seem to be no reason for specially lenient treatment. The insurance business, however, is often carried on on the mutual plan. In such cases, it is argued, insurance is not a profit making institution. Its function is to distribute losses, so that the burden will fall where it can best be borne. Life insurance companies are very commonly mutual, and even when they are joint stock the capitalization is as a rule relatively small and dividends on the stock are limited. Other forms of insurance, especially fire insurance, are likewise very frequently provided on a mutual basis. In the case of fraternal insurance, conducted on the assessment plan, the validity of the argument seems to be admitted by our laws. It is argued that even when the fraternal features are absent, and fixed premiums are collected the same principles apply. It is concluded that mutual insurance at least should be exempt from special forms of taxation.

To this it is replied that life insurance at least is often used as a form of investment through the use of endowment policies and the like; and that there is no reason why this form of investment should be specially favored. Passing by the contention that insurance is so desirable from a social point of view that it should receive a measure of "protection," it should be noticed that the argument in regard to investment has little application under the conditions existing in this State, since in practically all other cases investment securities are not property for the purpose of taxation. The reasons for this policy are considered elsewhere.[7] Here it need only be pointed out that so far as justice is concerned the argument in favor of the exemption of securities applies with at least undiminished force in the case of insurance.

The chief justification for the taxation of mutual insurance, if there be any justification, is to be found in the fact that insurance companies are productive in the sense that they render a valuable service. This may be merely the distribution of risks or of losses, but it is nevertheless a real service. Those who take out insurance policies are presumably better off than they would otherwise be. From this point of view all insurance companies may be regarded as creating value, and therefore tax paying ability. Upon the whole, however, the taxing of insurance premiums seems to lack adequate justification.

The laws in regard to the taxation of insurance companies have, of course, no application to the system of compulsory industrial insurance that is carried on by the State itself. Nor can the payments which employers are required to make on account of it to be regarded as taxes. They are paid into the "accident" fund which is intended to be "neither more nor less than self supporting, exclusive of the expense of administration."[8] With this form of insurance the Insurance Department of the State has nothing to do.

§6. The laws providing for "privilege taxes" on the gross receipts of express and private car companies were passed by the legislature of 1907 on the recommendation of the State Board of Tax Commissioners. As in the case of insurance the term "company" is very broadly defined. The statutes relating to express and private car companies are substantially identical, save only that the rate is five per cent for the former and seven per cent for the

[7] pp. 26-7.
[8] Workman's Compensation Act (1911), Section 4.

latter. The law specifically provides that the tax shall be in addition to the general property tax and not in lieu of it.

Express companies are defined as those "engaged in the business of conveying to, from, or through this state, or any part thereof * * * any articles by express service as distinguished from the ordinary freight lines of transportation of merchandise and property. * * *." The tax is collected only from the large organizations commonly known as express companies, no account being taken of local "express" or "transfer" companies. This means that it falls upon but five companies: the Western, the American, the Northern, the Great Northern, and the Wells Fargo.

A private car company is defined as one operating freight cars over any railroad line or lines within the State which it does not itself own or lease. The act therefore applies not only to companies that are primarily engaged in this business, but to industrial companies that make use of their own cars. It applies, however, only to freight cars. Most of the great railroad companies own the sleeping, dining, and observation cars used on their lines. At the time the Commissioners recommended the adoption of the tax they found that there were only eight Pullman cars operated in the State and that these were already adequately taxed.[9]

The reason for the tax in both cases appears to have been the belief that the companies were escaping their fair share of the tax burden. The express companies had previously been taxed only on their tangible property, consisting of such things as office furniture, horses, and delivery wagons.[10] In 1906 the Northern Pacific (now the Northern) Express Company, the largest of the three then doing business in the State, was assessed at $26,841.25.[11] Its gross receipts for business done wholly within the State, no account being taken of that beginning or ending elsewhere, were $152,654.39. The Great Northern Express Company was assessed at $16,187.50, and its gross receipts from state business were $163,266.73. The Pacific Express Company was assessed at $3,451.00, its gross receipts from state business being $46,135.00. Taxed only on their tangible property, all the express companies paid in 1906 for all purposes only $451.37, and in 1907, $750.26. In 1913, the last year for which the figures are available, the express companies paid under

[9] 1 Tax Commissioners, p. 120.

[10] Ibid., p. 105.

[11] These and the following figures are taken from the Biennial Reports of the State Board of Tax Commissioners.

the general property tax but $1,080.89. At the time of their investigation the Commissioners found that the private car companies had previously paid no taxes whatever in this State.[12]

Beginning in 1908, the first year in which the privilege taxes were imposed, the tax on the gross receipts of express companies has increased from $41,977.45 to $58,031.84. The yield of the tax on private car companies has been small. During the same period it increased from $595.86 to $1,455.94. In individual cases it is ridiculously small. In 1914 the Garden City Milling Company paid a tax of four cents, and ten of the forty-five companies paid less than $1 each. Only five paid more than $100, the largest being $311.18 paid by the Union Tank Line.

The privilege taxes are assessed by the State Board of Tax Commissioners in much the same way as are the taxes on the operating property of railroads and telegraph companies. The companies are required to file sworn declarations, covering the year ending April 1st. In this case there is a penalty of $500 for failure to file the declaration and an additional penalty of $100 a day for delay after April 30th. These declarations are checked by reference to the findings of the Public Service Commission, and by hearings to which the companies are entitled to send representatives. The Commissioners have the power to summon witnesses and to examine books and papers. Since only the receipts from business beginning and ending in the State are taxed there is no special difficulty in regard to the distinction between interstate and intrastate business.

The Commissioners, having ascertained the gross receipts on state business for each of the companies, make a report to the State Treasurer, who computes and collects the tax. In this case, as in that of the general property tax, interest at the rate of fifteen per cent a year is charged on delinquent taxes.

For several years the companies paid the privilege taxes without serious protest. In 1913 the Northern Express and the Great Northern Express companies carried the matter to the courts, alleging that the tax was unconstitutional, being an interference with interstate commerce. The Superior Court of Thurston County took this view of it and the decision was affirmed by Department No. 1 of the Supreme Court.[13] In a rehearing by the Supreme Court, sitting *en banc,* the cases of the two companies being combined, the deci-

[12]Tax Commissioners (1908), p. 13.
[13]76 Wash. 636.

sion was reversed.[14] All the companies concerned, with two relatively small exceptions over which the State cannot exercise jurisdiction, have now paid the tax, the Northern and the Great Northern Express Companies doing so under formal protest.

The decision of the State Supreme Court, upholding the act, was handed down in a divided court, there being four separate opinions, one concurring and two dissenting. The act was upheld on the ground that the tax was levied only on the gross receipts from business done entirely within the State, the interstate companies being under no obligation to do this business. The dissenting justices objected to the view that an express company might refuse to do an intrastate business, and one of them argued that the act applies not only to such business, but also to the State's share of the interstate business.

§7. There is perhaps no form of business in the United States that, where it is legally permitted to exist, is more commonly subject to license taxation than that of dealing in alcoholic liquors. Washington has heretofore derived a very considerable revenue from this source, notwithstanding the fact that for some years a system of local option has prevailed and many parts of the State have been "dry." In 1914, however, an initiative law providing for state-wide prohibition after January 1, 1916, was passed by a large majority. It will be worth while, however, to consider briefly the former situation.

Incorporated cities, towns, and villages had the exclusive right to regulate or prohibit the sale of alcoholic liquor within their corporate limits. Outside of these limits similar power was vested in the counties. In either case, however, if licenses were issued a tax of not less than $300 nor more than $1,000 a year was imposed. Of this, ten per cent went to the State, and no license might be issued until the State's share was paid. In 1914 the State received $131,179.34 from this source.[15]

In addition to the local liquor license taxes there was a state tax of $25 a year imposed on all dealers, including steamships or other vessels, dining cars, buffet cars, etc. Where the cars were operated partly within and partly without the State the number of licenses had to be equal to the average number of such cars within its boundaries. Receipts from this source for the year ending September 30,

[14] 80 Wash. 309.
[15] Figures furnished by State Treasurer.

1914, amounted to $59,462.26.[16] During the last few years they showed a tendency to diminish, due, no doubt, to the increase in the number of "dry" localities.

The hardship resulting from the loss of revenue from liquor licenses would be more apparent than real if there were no constitutional difficulties in the way of adopting a system of taxation suited to modern conditions. Perhaps it will prove so even as things are. The taxes collected by the State and its subdivisions must, with a few qualifications that are of little or no importance in this connection, come from the incomes of the people. There is no reason for thinking that the revenues needed will be increased by prohibition, or that the incomes of the people will be materially reduced. Some capital has doubtless been lost and it is possible that some has left the State. The amount of this, however, should not be exaggerated. Much of the property used in the liquor business could be used in other lines of industry. If the prohibitionists are right in thinking that the liquor business is unfavorable to health and efficiency it may be expected that the incomes of the people will be increased. It must be admitted, however, that it is not easy to find taxes that are as easily levied and collected with as little opposition as are liquor licenses. This, however, is an administrative problem: it does not mean that the people will have to pay more taxes nor that they will have less with which to pay them. Even the administrative problem would be less difficult if it were not for the present defective system of taxation.

§8. Automobile licenses can be regarded as only in part business taxes. They will, however, be considered in this connection; partly because they seem to be, to some extent, intended to be business taxes; and partly because they are not of sufficient importance to be separately considered and there is no other group of taxes with which they can be more appropriately classed.

Heretofore automobiles have been taxed at a flat rate of $2 for each machine. In some respects this charge seems more like a fee than a tax. For the biennium ending September 30, 1914, however, the total amount received was $106,246,[17] whereas, as we have already seen, the total expenses of the office of the Secretary of State, who is responsible for their collection, were only $25,501.68. Even if a large part of these expenses are attributed to the automobile

[16] 5 Tax Commissioners, p. 37.
[17] 13th Biennial Report of the Secretary of State (1914), p. 10.

department, it would seem that the automobile licenses contain a large element of taxation.

The Legislature of 1915 adopted a fairly elaborate system of automobile licenses. Without giving the schedule in full it may be said that there are seven classes of automobiles, the classification based partly on the kind of machine and partly on the use to which it is put. On motor cycles there is a flat rate of $2.50; private "automobiles" are subclassified on the basis of horse power, the rates being $3, $5, and $7.50; on "automobiles for hire" the rate is fifty cents per horse power; motor trucks are subclassified on the basis of capacity, the rates being $10, $15, $20, and $25, with, apparently, no provision for those having a capacity of more than five tons. On auto-stages the rate is fifty cents per horse power and $1 per passenger capacity; on demonstration machines the rate is $3 for motor cycles and $5 for all others. Except for motor cycles there is an additional demonstration license of $3. Private automobiles may be licensed for hire for ten days or less on payment of a license of $1. In addition to these there are small fees for duplicate number plates and licenses and for the transfer of licenses.[18]

The new system may be expected to yield a considerable amount of revenue. Licenses are to be collected by the Secretary of State through the county auditors, and turned over by him to the State Treasurer. From these receipts the general fund is to be reimbursed for expenses incurred and the remainder is to be turned into the permanent highway fund, these payments to be in addition to fixed appropriations.

It will be readily seen that, from one point of view, automobile licenses might be regarded as fees for the use of the roads. The maintenance of highways, however, is commonly regarded as one of the general functions of the State. Upon the whole it is better to regard such licenses as for the most part taxes on particular classes of citizens who are supposed to have special tax paying ability and also to receive a special benefit from the way in which most of the money thus received is expended.

There are, of course, many other cases in which charges are imposed by the State upon business. These are so largely in the nature of fees or prices that a discussion of them in a work of this sort is unnecessary. Special mention should be made of the fishing industry in which there are a considerable number of fees.

[18]Session Laws of 1915, Ch. 142.

Chapter VIII.

THE INHERITANCE TAX

§1. The taxation of inheritances, using the term in a broad sense, has grown greatly in favor among American commonwealths during the last generation or so. The Washington inheritance tax law dates back to 1901. It was considerably revised in 1907, though no changes in the rates, that have stood the test of constitutionality, were made. Previous to its administration by the State Board of Tax Commissioners, beginning in 1906, the amount of revenue produced was small. It has increased greatly since that time and may be expected to increase in the future, though at a slower rate.

In providing for the taxation of inheritances the Legislature has a comparatively free hand. The tax is not technically on property, but on successions; and the constitutional provision in regard to the uniform taxation of property has no application. It is not a tax on interstate commerce nor on the instrumentalities thereof, and some of the most important constitutional difficulties that arise in the case of business taxation can here cause no trouble. This does not mean that there are no constitutional restraints, but they are much less frequent than in the cases of the other taxes that we have considered.

§2. Allowing for a few exemptions, the Washington inheritance tax is intended to reach all cases of the succession to property resulting from the death of the owner, so far as the State has any control in the matter. The term "inheritance" is, of course, interpreted as including bequests and devises. The law applies also to deeds, grants, sales, or gifts made in contemplation of death. When real estate is left to direct heirs for a term of years or for life with the provision that it shall then go to collateral heirs, the value of the term or life estate must be appraised and the tax paid upon it; and when the collateral heirs come into the property they must pay the tax in the same way as if it had passed to them in the first place. If, however, they wish to pay at the time of the death of the testator, the present value of their interest is computed and the tax paid on that basis. This part of the statute is very faultily drawn. Unless the intention is to grant exemptions—and this apparently is not the case—the distinction between direct and collateral heirs is cumbersome and uncertain. The Tax Commissioners rec-

ommended to the last session of the Legislature that the law be amended to remedy the difficulty, but nothing was done.

One of the chief faults of the inheritance tax, as administered by American commonwealths, is double taxation, since many of them impose it wherever possible. In this respect Washington is a grievous offender. The tax is imposed when the property is in the State and distributed under its laws. Except in the case of real estate passing in fee, the tax is imposed when the property is located elsewhere but the decedent was domiciled in Washington at the time of his death. Even if the decedent was a non-resident and the property located outside of the State the tax is imposed when it is brought in and becomes subject to the courts of the State for distribution. Domestic corporations are forbidden to transfer securities subject to the tax at the request of foreign executors, administrators, or trustees until payment has been made under penalty of themselves being liable. Finally, safe deposit companies, banks, and other corporations or persons, holding securities, property, or assets are forbidden to transfer them to non-resident executors, administrators, or trustees under penalty of themselves being liable.

§8. While students of taxation are generally agreed that but one state should collect the inheritance tax on the same property there is some difference of opinion as to which it should be where several put in a claim.[1] It is ordinarily conceded that in the case of real estate the tax should be imposed by the state in which the property is located; but in the case of personal property there are three or four possible claimants.

One view is that since the tax is laid on succession it should be imposed only by the state under the laws of which the privilege is secured. This, in the case of real estate, is the one in which it is located; in the case of personal property the one in which the decedent was domiciled.[2] This view seems reasonable. At the same time it must be remembered that it is not property but persons that owe taxes. The state in which the recipient of the inheritance lives has a claim upon him to pay taxes according to his ability, and this ability is increased by reason of the inheritance. The state in which even personal property is located has some claims upon the owner, since the property is under the protection of its laws.

[1]For a good discussion of the subject, showing several different points of view, see 6 National Tax Asociation, pp. 283-320.

[2]Report of the Committee on Double Taxation and Situs for Purposes of Taxation, 8 National Tax Association (1914), p. 235.

To reach a satisfactory conclusion would require a somewhat deep theoretical study.[3] As a practical solution of the question it has been suggested that a compromise be made. Upon any particular compromise, however, it is difficult, and perhaps impossible, to secure agreement. The committee of the International Conference on State and Local Taxation appointed to draw up a model inheritance tax law recommended that the tangible property be taxed where located and the intangible property at the domicile of the decedent.[4]

This suggestion, like the one that the tax should be laid by the state in accordance with whose laws the property devolves, would, if accepted, do away with the evil of double taxation. The difficulty is that either of these plans would be more favorable to the older and wealthier states than to the others, since so much of the property in the newer and less developed states is owned by corporations whose stock is held by non-residents. These states are naturally unwilling to consent to any such arrangement.

While no really satisfactory conclusion seems to be at hand, it should be emphasized that the question is really a moral one. In practice it would seem that a very important consideration has been that the states have needed the money and the inheritance tax furnishes an easy way of getting it. The strength of this feeling is in part due to the very defective systems of taxation already in use and in part to the fact that the revenues needed are so large that any system of taxation would seem burdensome. One of the chief functions of the state, however, is to secure justice; and the present arrangements are clearly unjust. More discussion is needed; but it should be guided to a greater extent by a desire for justice and to a less extent by a desire for the money.

There is one step in the right direction which can be taken without waiting for agreement. Whatever arrangements a state makes should be such that if adopted by all double taxation would not result. If, for example, a state taxes tangible property within its borders when left by a non-resident, it should not tax tangible property located elsewhere but left by a resident decedent. In this respect the laws of Washington are in great need of reform.

§4. While the Washington law is far reaching there are a few exemptions. Bequests of property within the State for the relief of aged, indigent and poor people; for the maintenance of the

[3] On the whole question of double taxation see Seligman, "Essays in Taxation" (8th edition), Ch. IV.
[4] 4 National Tax Association (1910), p. 284.

sick or maimed; or for the support or education of orphans or indigent children are entirely exempt. Besides this an exemption of $10,000[5] is allowed for direct heirs. There are no other exemptions.

That part of the statute which deals with the exemption of charitable bequests could be greatly improved. It is not charitable institutions that are exempt, but bequests for a very limited number of purposes. If property be left to an institution that is primarily charitable, but has other purposes than those specifically mentioned, the question arises as to whether or not the property will be used exclusively for the prescribed purposes. If, for example, it be left to a hospital that receives a large number of free patients, but makes a charge to those that are able to pay, this question arises. In practice the law seems to be administered in the light of reason. Under any reasonable interpretation the exemption is very narrow. There are many institutions that are founded for other purposes than those mentioned, are maintained solely for the public welfare, and are almost altogether dependent for their support on gifts and endowments. Inheritance tax laws commonly provide for the exemption of religious, educational, and charitable institutions; but here, with the exceptions already noticed, they are taxed at a rate varying from six to twelve per cent. Apparently even a bequest to a state institution would be taxed. This has actually happened in the case of a school district.

The exemption of $10,000 to direct heirs would seem rather small where the widow is entirely dependent on property left by the husband, were it not for one important fact which is commonly overlooked in discussions of the inheritance tax. Property acquired by either husband or wife, subsequent to marriage, except that acquired by gift, bequest, devise, or descent, with rents, issues, and profits thereof, is community property.[6] Upon the death of either party the survivor becomes the owner of one-half of it, and this half is not subject to the inheritance tax, though it must bear its share of the costs of closing the estate. Minor children, of course, have no claim on the community property, and where they are left orphans the exemption seems small. In other cases it seems somewhat larger than is necessary. It must be remembered, however, that for this class of heirs the tax on amounts in excess of the exemp-

[5] In connection with the tables published in the volumes of the National Tax Association (IV, 289; V, 307; VI, 293) it is stated that there is an exemption of $15,000 to the widow and $10,000 to each other lineal descendant. This is clearly an error.

[6] Rem. and Bal. Code, Vol. II, Sections 5915-5917.

tion is at present only one per cent. If, therefore, the amount involved were as much as $20,000 the tax would be only one-half of one per cent.

There is, however, one fault that would be serious if the rate were at all high. The exemption is not granted on each share, but on the entire property passing to heirs of this class.[7] This may be good law, but it is wrong in principle. The tax should rightfully be regarded as resting on the recipients of the property.[8] The exemption is best justified on the ground of the hardship involved for those who previously had some claim on the decedent and now receive only a small sum from his estate. It would seem, therefore, that the exemption to each should depend, not on the size of the estate, but on the amount that each beneficiary receives. It is true that where the inheritance went to a family group a larger exemption could be gained by dividing the estate among the members of the group; but the larger the group the greater is the need of exemption.

In the case of collateral heirs the Washington law allows no exemption. To this there can be little objection. Normally collateral heirs are not dependent in life on the person from whom they receive a bequest. It would, perhaps, be well if it were possible to make provision for exceptional cases. Aside from this, especially when the rate of taxation is low, justice does not seem to call for any exemption. It might, however, be well to allow one low enough to cover the case where the amounts are so small as to be hardly worth the trouble of collecting.

§5. As regards rates, the Washington tax, at the time it was adopted, was one of the best in the country. The idea of inheritance taxation, however, has since then received considerable development in American states, and there are now some improvements that might be made.

For the purpose of the tax the recipients of inheritances are divided into three classes. The first is that of direct heirs and is defined as consisting of father, mother, husband, wife, lineal descendant, adopted child, and lineal descendant of adopted child. Except for parents the law seems to make no provision for ascendants. No mention is made of grandparents and in practice they are treated as

[7] 1 Tax Commissioners (1906), Instructions and Opinions, p. 228.

[8] "The inheritance tax, while not a debt of the testator, was properly chargeable to the beneficiaries." In re Lotzgesell's Estate, 62 Wash. 352 ff.; for a discussion of the point see Seligman, "Essays in Taxation" (8th edition), Ch. V, especiallly p. 130.

collateral heirs, being grouped with brothers and sisters. Sons and daughters in law are treated as strangers to the blood. The second class of heirs includes collateral relatives to and including the third degree, that is, as far as uncle, aunt, nephew, or niece, inclusive.[9] All others are put in the third class.

The rates imposed can best be shown by a table:

Heirs	Exemption	Amounts above exemption		
		First $50,000	Second $50,000	Above first $100,000
Father, mother, husband, wife, lineal descendant, adopted child, lineal descent of adopted child.....	$10,000	1%	1%	1%
Collateral relatives as far as uncle, aunt, nephew, niece, inclusive....	0	3%	4.5%	6%
Other collateral relatives and strangers to the blood.....	0	6%	9%	12%

It will be noticed that for direct heirs the rate is progressive only so far as the exemption introduces an element of progression. On all amounts in excess of $10,000 the rate is one per cent. For collateral heirs of the first class the rate progresses from three to six per cent, and for all others from six to twelve per cent.

In 1907 there was inserted in the law a provision that in the case of non-resident alien collateral heirs the rate should be twenty-five per cent. This provision, which certainly seems unfair, was very soon found to contravene a treaty between the United States and the United Kingdom of Norway and Sweden.[10]. As this treaty was more favorable to an opposite construction than were the treaties with most other countries, the provision was repealed in 1911.[11]

§6. The inheritance tax could be made to yield more revenue if the rate on direct heirs were made progressive. This is done in a number of foreign countries, including England and France, and, especially in recent years, in a number of the American states. Since property commonly passes chiefly to direct heirs the rates actually collected are usually small. It is true that the immediate family may properly be regarded as having some claim on the estate; but it

[9]In reckoning consanguinity Washington follows the civil, instead of the common, law. Remington and Ballinger's Code, Section 1347.

[10]In re Peder G. Stixrud's Estate, 58 Wash. 339.

[11]3 Tax Commissioners (1910), p. 9; Remington and Ballinger's Code, Vol. III, Section 9183.

must be remembered that, as a matter of necessity, taxes are generally imposed on wealth to which the taxpayer has a just claim. It is true that the death of a member of a family is likely to mean financial loss to those that remain; but, on the other hand, the expenses of the family are likewise commonly reduced. Where the income of the family has previously consisted chiefly of the personal earnings of the deceased there is a real financial loss. If there were no exemption the tax would work hardship in some cases and would be unfair. Where, however, there is a reasonable exemption and a low rate until the inheritance has reached a considerable amount, and especially where the surviving husband or wife, as the owner of one-half the community property, pays no inheritance tax on it, there seems to be no reason why a progressive rate may not be imposed. It must be remembered that where the inheritance is large the personal earnings of the deceased have commonly been a smaller factor in the life of the family than when the inheritance is small.

The determination of the rates to be imposed must, in the present state of our knowledge as to the actual effects of the tax, be more or less arbitrary. Probably four or five per cent, as a maximum, would not be excessive, but it should be applied only in the case of a very considerable inheritance. The model inheritance tax, outlined by the committee of the International Conference on State and Local Taxation,[12] provides for an exemption of only $2,500 in the case of direct heirs and a tax upon them increasing from one to four per cent, the points at which the rates increase being $25,000, $250,000, and $1,000,000.

The rates imposed on collateral heirs are less open to adverse criticism. The maximum rate is twelve per cent. While in some states and in some foreign countries the maximum is considerably higher, it may be doubted whether, under existing conditions, it should be more than fifteen per cent. This is the maximum imposed by California and Wisconsin and it is that recommended by the committee on a model inheritance tax to which reference has already been made. The rate in these cases, however, increases more gradually than it does in Washington, and in the two states mentioned the maximum is applied only to amounts of more than $500,000. The committee on a model inheritance tax recommended that the rate of fifteen per cent be applied only to amounts in excess of $1,000,000.

[12] 4 National Tax Association (1910), p. 286.

In providing for two classes of collateral heirs Washington goes beyond the recommendation of the committee on a model inheritance tax, but not as far as the practice of a number of the other states, including Wisconsin and California. In the opinion of the author two classes are desirable and sufficient; and the Washington tax could hardly be improved in this respect.

We have seen that treating the exemption of $10,000 in the case of direct heirs as a single exemption to the estate is wrong in principle, and may result in serious hardship in practice. Much the same might be said—and more strongly—of making the rate, where the tax is progressive, depend not on the size of the particular inheritance, but on the size of the estate. It is chiefly because ability to pay increases with the increasing size of the inheritance that a progressive rate should be imposed. The ability of the recipient is dependent, not on the size of the estate, or the amounts passing to other heirs, but on the amount passing to him. In this matter the Washington tax is capable of improvement.

§7. As has already been mentioned the State Board of Tax Commissioners is charged with the supervision of the inheritance tax. Executors, administrators, and trustees are required to send to the Board, on demand, certified copies of any parts of their reports. The Commissioners have authority to institute court proceedings whenever necessary and the county attorneys are required to render assistance. The Board keeps memoranda of such proceedings and an itemized account of all taxes collected, charging them against the State Treasurer.

When any petition for letters of administration or probate of will are filed the petitioner is required to furnish the clerk of the court with a statement of the location, nature, and probable amount of the entire estate, a list of heirs, etc., with the relationship of each to the decedent, and an estimate of the amount or value of each share. A copy of this list, with certain other information, is forwarded by the clerk of the court to the Tax Commissioners.

The appraisers of an estate for inheritance tax purposes are appointed by the court, and are usually the same as those appointed under the probate law. The appraisers give notice to the Commissioners of the time and place of making the appraisal. The latter, or any persons interested, may file exceptions, which shall be heard and determined by the court.

In order to ascertain the amount of the estate liable to the tax certain deductions must be made. These are debts owing at the time of death, including state and local taxes, a reasonable sum for funeral expenses and court costs, and the statutory fees of executors, administrators, and trustees. In the case of a foreign estate, liable in whole or in part to the tax, similar deductions are allowed upon the submission of proper evidence.

When the property charged with the inheritance tax is of such a nature or so disposed that the liability is doubtful the Commissioners have authority to compromise with the beneficiaries or other representatives of the estate. To be valid, however, such compromise must be approved by the court having jurisdiction of the case.

The inheritance tax is ordinarily collected through the executors, administrators, or trustees. It must be paid within fifteen months from the date of death unless the time is extended by the court. In the case of real estate, failure to pay the tax within the time allowed may result in a court order directing that the property, or as much of it as is necessary, be sold and the tax paid. As we have already seen, a domestic corporation transferring stock at the request of a foreign executor renders itself liable for the tax and, in like manner, anyone holding securities or other property of a non-resident delivering such property to a non-resident does so at its own risk. Payment of the tax is made to the State Treasurer, who issues a receipt in duplicate, one copy of which is filed with the Tax Commissioners.

To deal with the numerous cases in which the only necessity for probate is the determination of the liability of an estate to the inheritance tax the Commissioners recommended to the last session of the Legislature the passage of a law providing for a simple and inexpensive method of procedure.[13] They also recommended a law for the appointment of public administrators to deal with cases where there is no relative residing within the State and entitled to make application for letters of administration.[14] Neither of these laws, however, met with the approval of the Legislature.

§8. For the first few years after it went into effect the yield of the inheritance tax was small, but since then there has been a very great increase. For the four years ending June 13, 1905, the total

[13] 5 Board of Tax Commissioners (1914), p. 26.
[14] Ibid., p. 24.

receipts were only $53,175.35[15]. For the biennium ending September 30, 1914, they were $291,888.65. This is a little less than for the preceding biennium when they were a little more than $300,000.

The great increase in the revenue is doubtless to be accounted for in part by the increased number and value of estates properly subject to the tax; but such an explanation would seem to be quite inadequate for an increase as great as that which has taken place. It appears that until the organization of the State Board of Tax Commissioners, in 1905, there was no one who was directly responsible for its collection.[16] The powers of the Commissioners were increased in 1907, and they then began an examination of the probate records to find cases in which the tax was delinquent. At the time of their report in 1908, though the investigation was not quite completed, there were more than two thousand cases still unsettled, in some of which the delay was due to legal questions which had not been settled.

There is, of course, still some evasion, the amount of which it is impossible to determine. The inheritance tax is commonly thought of as one that is relatively easy to enforce and while this is doubtless true there are some serious difficulties. When property passes through the probate courts it can, of course, be found, but, as in the case of the general property tax, there are often difficulties of valuation. These difficulties are usually less than in the case of the general property tax, for it is practicable to examine each case more thoroughly. The work is not done by poorly paid deputies who have much property to examine. The property is in the hands of executors or administrators who ordinarily have much less interest in keeping down the valuation than has the owner of property in dealing with the assessor. In many instances, though by no means in all, the appraisal is made for purposes of distribution as well as for purposes of taxation. The whole matter is under the eyes of the court, and there are often beneficiaries whose interest it is to see that the estate is correctly valued.

Property that is legally subject to the inheritance tax does not necessarily pass through the courts. It is here that ante-mortem gifts are important. In the case of personal property there need be no record of the transfer, and the State is largely dependent on

[15]Figures used in this connection are from the Biennial Reports of the State Board of Tax Commissioners.
[16]2 Tax Commissioners (1908), p. 28.

the willlingness of those who have received it to acknowledge the obligation. In some cases large estates are incorporated and the stock is transferred under circumstances which make it impossible to prove that it is liable to the tax.

Of course it is possible to avoid the inheritance tax, as it is to avoid any other, by establishing a residence elsewhere and having no property invested in such a way that the courts of the State can reach it. If the tax were very heavy it is probable that this would be done in some cases, especially in the case of those possessed of very large fortunes. Here, as in so many other cases of taxation, it is the wealthy who are best able to escape. It is very doubtful, however, whether the Washington tax is sufficiently severe to produce much effect of this sort.

§9. Unlike the general property tax the inheritance tax is thoroughly sound in principle, and there seems no reason to doubt that it can be so administered as to work well in practice. Like any other tax it has its limitations. If the rate rises above a certain point evasions will increase; and it is not impossible that wealthy citizens will leave the State. If these difficulties were successfully met a very high rate would not improbably check the accumulation of wealth; and it must be remembered that economic prosperity is largely dependent on capital. Even if the rate be not too high grave injustices are possible. Reference has already been made to the double taxation resulting from the attempt of different jurisdictions to reach the same property; to the treatment of exemptions as applying to the estate as a whole and not to the different shares; and, in like manner, to the determination of the rate where the tax is progressive, by the amount of the estate instead of by the amount that each beneficiary receives. These evils, however, are not inherent. They could be eliminated by proper legislation and a good, effective tax remain.

Chapter IX.

THE REFORM OF THE TAX SYSTEM

§1. In considering possible improvements attention will here be given almost exclusively to the general property tax and to some of the possible substitutes for it. Not only is it the most important element in the present system, but it is the one that presents the greatest difficulties to reform. Most of the taxes on business are merely supplementary to it or are largely in the nature of fees. The inheritance tax could doubtless be improved in some matters of detail, as was pointed out in the last chapter; but the fundamental principles on which it rests are sound.

§2. The assessment of property could undoubtedly be made much more accurate than it is. As has already been pointed out[1] the administrative machinery is seriously defective. Difficult and important as is the work of the assessor his office is a political one, his tenure is short, and his remuneration is small. Not only should all these conditions be changed but the work of assessment should be organized for the State as a whole.

Almost any tax can be collected if the rates are sufficiently low and the conditions are otherwise favorable. In those Swiss cantons in which it is most successful the rate on personal property for all purposes varies from four to seven mills in the case of large estates, with still lower rates for the smaller ones. In those cantons in which the rate rises above ten or twelve mills the attempt to collect the tax is a failure.[2]

Even in some of our American states a considerable amount of revenue is secured from the taxation of intangibles at a very low rate. This has long been true of Pennsylvania. In Maryland the rate was reduced to three mills for local purposes in 1896. Even with the state tax added the total was less than five mills. In Baltimore, which previously had a rate of twenty mills, the increase in the valuation was nearly ten-fold in the first year.[3] In 1911 Minnesota had a somewhat similar experience, the rate being reduced from an average of more than twenty-eight mills to three mills. In

[1] pp. 41-2.
[2] Bullock, "The General Property Tax in Switzerland," 4 National Tax Association, pp. 55-84. See also Seligman, "The Income Tax," pp. 355-363.
[3] Hollander, "The Taxation of Intangible Wealth in Maryland," Quarterly Journal of Economics, Vol. XXII (February, 1908), pp. 196-209.

this case the change in the rate was accompanied, as of course it should be, by an improvement in the methods of assessment.[4] There seems no sufficient reason to believe, however, that in either case a really satisfactory assessment is made.

Assuming, however, that with good assessing machinery and a very low rate of taxation the general property tax could be effectively administered, this would hardly solve the problem. The state and the localities need considerably more revenue than could be raised by the general property tax at any such rates as those that have just been mentioned.

§8. Considering the numerous efforts that have been made at many times and in many places to make the general property tax work well and the exceedingly small degree of success that has attended such efforts there is at least ground for suspicion that the fault does not lie wholly in the wickedness of the property holders, or even in this together with the inadequacy of the methods of assessment. At the Fourth International Conference on State and Local Taxation a committee appointed to examine into the causes of failure ended its report with the following words[5]:

"We conclude, therefore, that the failure of the general property tax is due to inherent defects in the theory;

"That even measurably fair and effective administration is unattainable; and that all attempts to strengthen such administration serve simply to accentuate and prolong the inequalities and unjust operation of the system."

There is little reason to doubt that the committee was right in its view of the matter. The general property tax is fundamentally defective in theory. Even if it could be successfully collected it would be unjust. Every citizen should pay taxes according to his ability; but property, taken alone, is not a satisfactory criterion of ability, nor do all kinds of property represent ability in the same degree.

It should be sufficiently obvious that personal earnings furnish ability to pay taxes just as truly as does the income from property. A system that taxes the weak who are dependent on a small amount of property and exempts the strong man who earns a large income from his profession but promptly spends it all is clearly unjust. It is doubtless true that the income from property is, as a general proposition, less precarious than that from personal earnings, and

[4] Armson, "Two Years' Experience in Minnesota with the Three Mill Tax on Money and Credits," 6 National Tax Association, pp. 243-245.
[5] 4 National Tax Association, p. 310.

that it does not cease with the death of its owner. It may also be conceded that the wealthy man who could, but does not, take an active part in industry has more ability than the man who, by hard work, earns an equal income. Such considerations as these may justify a higher rate of taxation on the income from property than on that from personal exertions; but they assuredly do not justify the exemption of the latter, especially when the needs of the state are so great as to make necessary a very high rate of taxation if it is confined to property.

The same difficulty is brought out when the taxation of business property is considered. Even in any given line of industry profits are not dependent on the amount of capital alone, but on the ability with which it is used and on special considerations of the sort that are commonly spoken of as good and bad fortune.

Some forms of property yield no income at all except that of personal enjoyment to the owner. Of two men in receipt of the same income one may spend a portion of his for durable sources of satisfaction, the other for those that are transitory. The former may possibly get more real enjoyment out of life than the latter, but it is not by reason of benefits conferred by the state nor by reason of taxpaying ability. In fact he may have less ability. The man with family responsibilities is more likely to own his own home, which is one of the things most easily taxed. Even if it be true that taxes on buildings are generally shifted such a man ordinarily occupies larger premises than the man who has no such responsibilities.

In some cases the general property tax is defective, not so much by reason of the amount of taxes as by the circumstances under which they are collected. In the case of forests, for example, no income may be received for a long period of time, and owing to the danger of fire and the other uncertainties of the future the amount that will eventually be received may be very uncertain. Yet the forest has a present value, dependent on its anticipated value, discounted for time and for risk. Probably no one would deny that it should be taxed, and taxed at a fairly high rate, but there is at least very serious question whether the method should be that of the general property tax.

§4. It may possibly be thought that the inequalities will be smoothed out through the shifting of taxes. To some extent this is indeed the case; but as a general proposition it is not true. Even

when shifting takes place it is usually very difficult to follow; and the extent to which the injustices are removed may be impossible to ascertain.

It must be remembered that, as a rule, shifting takes place only when demand or supply is affected. A tax laid on one particular line of business or one particular form of investment, if effectively administered, will generally be shifted because, other things being equal, enterprise and capital will seek those lines in which the burdens are least. If all were taxed alike the taxes would be shifted only so far as enterprise was discouraged from activity; and the extent to which this will happen is almost impossible to determine. When the tax is uncertain in its operation shifting is less likely to take place. One of the chief questions in that case is whether or not the particular individual will happen to be caught. So far as the fear, of the typical business man, influences his actions it may have some influence on the incidence of taxation; but what the effect will be is largely an unknown quantity.

Shifting doubtless tends, to some extent, to smooth out the inequalities between different lines of business. It can hardly smooth out the inequalities between different concerns. There is no assurance that it results in anything like the adequate taxation of those whose ability is derived from other sources than the ownership of property. Even if successfully administered a property tax is almost necessarily unequal in its operation.

Even if the burden were fairly distributed a serious evil would remain. A tax is direct, in the economic sense, only so far as it is not shifted. When the tax is indirect neither those who pay it in the first instance nor those who pay it in the last are likely to give to efficiency and economy in public expenditure the attention that a proper regard for their own interest would demand. The former see that the tax does not come out of their pockets. The latter do not realize the nature of the burden.

§5. Great as are the evils of the general property tax, Washington, like many of the other states, is firmly bound to it by its constitution. As we have already seen, the provisions in regard to exemptions are narrow and are strictly construed. The decision that virtually permits the exemption of intangibles may probably be regarded as an exception. Here the Court seems to have made use of the light of reason, in one of the best senses of that misunderstood term; but neither the light of reason nor anything else that

is legitimate, save only a constitutional amendment, will, so far as can now be seen, permit the adoption of anything like a satisfactory system of taxation.

Since it was organized the State Board of Tax Commissioners has never failed to recommend to the Legislature the submission of a constitutional amendment. In 1907 the recommendation was accepted, but the proposed amendment was defeated at the polls, partly at least, because it was not understood. The amendment recommended at the last session was allowed to die in committee.

All of the amendments proposed by the Commissioners would have given the Legislature, or since the use of the initiative and referendum became constitutional, the people acting directly, a fairly free hand. An essential feature of each of them was that which would permit the classification of property for the purpose of taxation. To some it will seem that any of them would give too much freedom; to others that they are all unduly restrictive. Which view will be taken will depend very largely on the attitude of its proponent towards constitutional government.

It may be admitted that under any of these proposed amendments various injustices would be possible. Under the existing constitution injustices are actual, and no modification of the general property tax that would remove them can be made. One need not be an enthusiastic believer in democracy to hold that it is highly improbable that evils worse than those that now exist would arise. It is true that various plans, the adoption of which would almost certainly prove unfortunate, to use a very mild term, are from time to time suggested and obtain a considerable following. To a very large extent they simply represent the reaction against the iniquities of the present system. Injustice is an excellent fertilizer for crude, incomplete, and exceedingly radical theories; and many of these movements would be weakened, if not killed, by the adoption of a more just system. If the general property tax is to be continued there is at least the danger that some of these movements will increase in strength; and it is not beyond the bounds of possibility that we shall be forced to put them to the test of experience, however costly that experience may prove to be.

If it were possible to provide constitutional restraints that would at once prevent injustice and allow the freedom that is necessary for the adoption of a satisfactory system it would, in the opinion

of the author, be desirable to do so. It seems fairly clear, however, that this is impossible. Even if it were proper to insert bodily in the constitution all the features that a good system under the present circumstances should have, the necessary flexibility would be lacking. We have at present cast iron provisions which were doubtless meant to secure real equality, but in this they have been an egregious failure. Sooner or later a change will come. To maintain a dam of constitutional restraints, such as we now have, is to take the grave risk that the demand for reform will eventually, like a disastrous flood, sweep all before it.

§6. No attempt will here be made to set forth a satisfactory system of taxation. He would be rash who undertook such a task single-handed. The matter should be examined from several points of view, and a number of considerations other than those with which the economist is primarily concerned should be taken into account. Probably complete reform must come slowly; but after the first big step—the amendment of the constitution—great improvement is possible.

One of the plans most widely favored in other parts of the country is the classification of property for the purpose of taxation. The number of classes need not be large, especially if entirely different methods are adopted in certain cases in which property is a particularly unsatisfactory basis for taxation. Many of those who advocate this system would have only three classes: real estate, tangible personalty, and intangibles. Probably, however, a somewhat more elaborate classification would prove desirable.

The most satisfactory part of the general property tax is that which has to do with ordinary urban and rural real estate; and this part might be left substantially untouched except for improvements in the method of assessment. Property of this sort now yields about eighty-five per cent of the revenue secured under the general property tax. Logically, it would seem that a distinction should be made between land and buildings. Land is generally admitted to be a particularly good subject for taxation. There is a more direct relation between public expenditures and the benefit received by the owner than is the case with almost any other form of property; and these benefits, as a general proposition, are of a sort that increases taxpaying ability. Moreover, even when the present owners have paid full value, the anticipated rate of taxation has been in a large measure capitalized and allowed for in the price that they paid.

To reduce the rate of taxation would practically amount to a gift to the present owners.

Yet even as regards land some distinctions should perhaps be made. Very probably forest lands should be put in a class by themselves. This does not necessarily mean that they should be taxed at a lower rate, but that they should be taxed by different methods. One very important suggestion that has been made is that an annual tax should be imposed on the land and a tax on the timber when cut, the latter being sufficiently high to make up for the period of exemption.[6] Such an arrangement as this should be made only with adequate safeguards and limitations. In particular some provision would have to be made to protect the various taxing districts, and perhaps the state itself, from irregularity in income. Strictly this plan need not provide for a separate classification of forest *land,* but the timber would have to be separately classified whether regarded as real or as personal property.

Mineral land might be put in a separate class. Like forest land there are special difficulties in the way of applying the general property tax to it. Possibly it would be practicable to distinguish between a mine as a piece of real estate, and a mine as a productive property, the former being treated in the same way as other lands.

It cannot be denied that there is an economic difference between land and those forms of wealth that are made by man, and that improvements are in the latter class. While, as a general proposition, capital should be taxed at a lower rate than land, it does not follow that this should be done in all cases, especially when there are serious practical difficulties to be taken into account. Such improvements as grading, when once made, become indistinguishable from the land itself; and even from the point of view of economics must often be regarded as land for many purposes. It appears that in Vancouver, B. C., which is supposed to use the "single tax" for municipal purposes, improvements of this sort are so treated soon after they are made.[7] Structures can, of course, be dealt with separately, and there is much to be said in favor of a lower rate of taxation than is applied in the case of land. Certainly, however,

[6] See Miller, "Forest Taxation in Washington," with the discussion following, in Taxation in Washington, pp. 45-68; Fairchild, "Suggestions for a Practical Plan of Forest Taxation," 6 National Tax Association, pp. 371-401; "Report of the Committee on Forest Taxation," 7 National Tax Association, pp. 413-422.

[7] C. J. Bullock, "The Single Tax in Vancouver," New York Evening Post, June 27, 1914.

they represent taxpaying ability, and there is no sufficient reason why they should be exempt unless this ability is reached in some other way. Indeed, there is some reason, from the theoretical point of view, for their taxation even when most forms of personalty are exempt, and it would seem that a higher rate on them would not be without some justification.

If the matter is to be considered from a practical, rather than from an ideal, standpoint it should be recognized that the tax on real estate, including structures, is one of the most effective parts of the general property tax. Any great reduction in the tax on buildings would necessitate radical changes elsewhere. Granting that there are evils in treating them in the same way as land, these are probably less serious than is the case with most other forms of capital. If a classified property tax is adopted it will be well to begin with a fairly simple classification. If this is done land and improvements may, at least for a time, be left in the same class.

§7. In regard to personalty the situation is different. It is here that the general property tax presents the greatest practical difficulties and the greatest theoretical defects. It is by no means certain that a considerable reduction in the rate of taxation would result in a serious loss of revenue. The fact that personalty represents only about fifteen per cent of the total valuation would alone justify the view that it would not. Moreover, the same fact at least suggests that the present rates on personalty are higher than the traffic will bear. It is not improbable that a material reduction in rates, accompanied by improved methods of assessment, would result in an actual increase in revenue.

Even if intangibles continue to be regarded as not property for the purpose of taxation, personalty should be divided into at least two classes: productive and unproductive property. Of the former almost any kind of business property is typical; of the latter, household goods. Productive property yields an income that furnishes taxpaying ability, though the special considerations that apply to land do not apply to it. For these reasons it should be taxed, but taxed at a lower rate than the land.

A few forms of productive property should probably be given special treatment, if only because of the difficulties of assessment. Public service corporations, for example, might be taken from under the property tax altogether. Some of the representatives of these corporations are emphatic in asserting their preference for a tax

on gross earnings. Commonly they have in mind such a tax imposed at a flat rate. This, however, would hardly be satisfactory. The rate should be adjusted, in some way, to the rate on property, and should vary with it.

Unproductive property is much less reliable as an indication of taxpaying ability than is productive property. The amount held is at least partly dependent on the individual's tastes and necessities. One man may spend much on travel, theatres, etc. Another may collect books and pictures. Doubtless the man who can afford to have a considerable amount of personal belongings is better able to pay than the one who cannot, but of two men of equal ability one may have a far greater amount of durable property than the other. Upon the whole it would seem that the tax should be less than in the case of productive property.

§8. In most of the states in which classification is desired it is largely in order that the intangibles may be separately treated, for it is here that the general property tax reaches the height of absurdity, both in theory and in practice. In Washington complete exemption has happily been preferred. If, however, it were possible to tax them at a low rate, the proposal to do so would undoubtedly be made. In regard to the merits of such a proposal there is something to be said on both sides.

The great underlying fact is that, with some exceptions that are of relatively little importance in this connection, credits are simply the right to receive tangible property that, presumably, is already subject to taxation. On this point the argument of our Supreme Court is thoroughly sound. If A mortgages land to B for $10,000 there is no increase of $10,000 in the wealth of the parties. Perhaps B rather than A should pay the tax on this amount, but to collect it from him does not necessarily mean that he is really the one who pays it. If C and D, previously transacting business as a partnership, incorporate and issue capital stock to the value of the tangible property, neither wealth nor taxable ability has been doubled. To tax both is to tax the stockholders twice; once collectively and once individually. Both taxes come out of the same earnings. This is commonly recognized where both forms of property are in the same state. The fact, however, that two states are involved does not remove the injustice; nor can a state that adopts a practice which, if followed by all, would inevitably result in injustice, claim that it is guiltless of the wrong.

Granting that the taxation of tangible and intangible property is double taxation, the argument for a moderate rate on the latter is not fully answered. It is quite possible that securities, taking into account the tangible property they represent, show a somewhat higher degree of taxpaying ability than does the direct ownership of tangible property, though clearly not as high a degree as would be necessary to justify taxation of both at the same rate.

It must also be conceded that equality, important as it is, is not the sole consideration. The fact that the tax on the property of the corporation is virtually only an indirect tax on the security holder is in some cases an evil, though in others the security holders probably realize well enough that the tax falls on them. Moreover it must be recognized that the community in which the security holder resides has some claim to taxes from him. In the absence of an agreement between taxing jurisdictions, which it may be impossible to secure, a certain amount of injustice is inevitable, whether intangibles be taxed or not. Looked at from this point of view a moderate rate is a compromise in an evil situation over which the state has nothing like adequate control.

There is no doubt that, with proper methods of administration, a large revenue can be secured from a low rate on intangibles. A few instances have already been cited. Experience in the East seems to show that the rate which can be successfully imposed does not exceed three or four mills. Notwithstanding the fact that interest rates are, at present, somewhat higher in the West than they are in the East five mills would undoubtedly put a heavy strain on the taxing machinery. Five mills may seem very small in comparison with the rates to which we are accustomed, but it must be remembered that this is really in addition to other taxes. Moreover, while some reasons have been advanced for the taxation of intangibles it should be recognized that they are not conclusive. There is much to be said in favor of continuing the exemption. If any tax is imposed it should probably not exceed three mills.

In considering the moderate taxation of intangibles a flat rate is commonly suggested. While it is generally desirable that the rate should fluctuate with public expenditures, a flat rate is less objectionable in this case than in most others, although it ignores, of course, the differences between different kinds of securities. Taxes on tangible property would still fluctuate, and these have their effect on the holders of intangibles. Moreover, the administrative ad-

vantages of a flat rate are probably greater in this case than in most others.

§9. The classified property tax has been discussed at some length, largely because of the very conspicuous part it would be sure to play, were the constitution amended, among the various proposals for reform. Our discussion should make two things clear: first, that the classified property tax would be a vast improvement over the present system; and second, that it would not be entirely satisfactory.

Classification of the sort here suggested is not arbitrary. It is based on economic distinctions between different kinds of property. To ignore them, as is done under the general property tax, is, to say the least, highly unscientific; and it is not at all surprising that as regards many kinds of property the present system works badly. Even under a classified property tax an improvement in the administrative machinery would be of vital importance; but it is doubtful whether any machinery could be devised under which the general property tax could be effectively administered. In view of the injustices that would result this is, perhaps, not wholly a matter for regret.

While the classified property tax, properly planned and administered, would do away with many of the worst evils of the present system some of them would remain. By classification allowance can be made for the very important difference between different kinds of property; but it is still a property tax. Property is but one test of ability. It may legitimately be used in conjunction with other tests; but used alone it fails to make allowance for the differences in the circumstances of individuals, except so far as this can be done through exemptions; and there are some important forms of ability which it reaches only indirectly and to a very uncertain extent, if at all.

As a method of reform the classified property tax has one great advantage over many others. It would be a big step forward; and the best progress is not ordinarily made by leaps and bounds. The change, though important, would not be violent in character; and there would not be serious difficulties of readjustment. It would require the adoption of no entirely new or unfamiliar methods. From the ground thus gained further steps could be taken. The method is that of evolution.

§10. While there are a number of possible substitutes for the personal property tax but one will here be considered. This is

the income tax. From some points of view it would be vastly superior to the classified property tax. Our brief experience with the federal income tax, however, may appear to many to furnish a strong ground for objection. In particular, great evils have arisen in connection with the principal of stoppage at the source; and there are a number of serious complexities.[8] The former can probably be removed only by an amendment of the law, and the same is true of a few of the latter. Some of the complexities, however, will be less troublesome after we become more familiar with the law. Many of these difficulties seem to have been avoided in Wisconsin, which is the leading state in regard to income taxation.[9] The Wisconsin law is really supplementary to that on real and tangible personal property, provisions being made to avoid double taxation. It would seem, however, that it would be possible to expand the scope of the income tax, diminishing that of the property tax till only the desirable features of the latter remain.

From the fact that we have a federal income tax both advantages and disadvantages in the use of a similar tax for state purposes would arise. Among the former are the possibilities in the way of efficiency in assessment and of convenience to the taxpayer. Probably the most important objection is the high rate that might be necessary if both the National Government and the State make use of the same tax. Even now the combined rate of the federal and Wisconsin income taxes, both of which are progressive, is very high in the case of large incomes, approaching thirteen per cent as a limit. The Wisconsin income tax, however, does not fall on the entire income.

Upon the whole the introduction of an income tax as a partial substitute for the general property tax would probably be the best possible method of reform. The tax on real estate, or at least on land, should of course be continued, and there are, perhaps, some forms of personal property that should still be subject to taxation. Double taxation resulting from the fact that both taxes are used is easily avoided. In Wisconsin the taxpayer is allowed to deduct his personal property tax from his income tax. Though not satisfactory as a single tax, there is much to be said in favor of making the income tax the central feature of the tax system. It

[8] See articles by C. J. Bullock, F. L. Speer, and A. C. Reardick, 8 National Tax Association, pp. 264-314, and the discussion following; also articles by M. L. Schiff and R. G. Blakey, Annals of the American Academy of Political and Social Science, Vol. LVIII (March, 1915), pp. 15-43.

[9] See articles by K. K. Kennan and T. E. Lyons, Annals of the American Academy, loc. cit., pp. 65-86.

reaches forms of taxpaying ability that hardly any other tax can reach and in regard to which the property tax is a very bad failure. Like the classified property tax, its adoption would not make necessary violent readjustments, and would open the way for the development of a satisfactory system.

§11. A possible reform of a somewhat different sort that is sometimes proposed is the adoption of "local option" or home rule in taxation.

It is, perhaps, not generally realized that a limited measure of home rule exists today. In particular, the cities have a large degree of freedom in their use of business licenses. So far as the law is concerned it would probably be possible for a city, even now, to largely abandon the general property tax for municipal purposes. This, however, is not what is commonly meant when home rule is mentioned. Under complete home rule the localities would have the power to devise their own systems of taxation. Commonly its advocates have the general property tax particularly in mind. They would permit the localities to classify property, to fix the rates, and, above all, to grant exemptions. The movement for home rule in taxation is in part a protest against the iniquities of the general property tax, in part a phase of the movement for the adoption of some particular reform, and in part a phase of the movement for home rule as a general political principle.

Regarding taxation as a means of securing revenue, the chief object with which we are here concerned is the discovery and application of a rule for measuring the taxpaying ability of individuals. If the methods of taxation are to rest on scientific principles it would seem that the state is in a much better position than the localities, especially the smaller ones, to handle the matter efficiently. Indeed, to leave it to the localities would involve a most unnecessary amount of duplication of work. It may be admitted that conditions differ in different places, and it is possible that what is best for one is not best for another; but it may be doubted that conditions are in fact different in such a way or to such a degree as to make this an important consideration. The suggestions that we have considered in regard to the form of taxation would seem to be of fairly general application.

A consideration which appeals very forcibly to the author is the fact that the interests involved are not so distinctively local as to make the methods of taxation anything like a matter of indifference

to other parts of the state than those directly concerned. It is not merely that each locality is interested in the welfare of the state as a whole. On the contrary, it is only too often willing to gain at the expense of others; and herein lies a part of the difficulty. Under home rule one locality might, by its competition, virtually compel others to adopt methods of taxation similar to its own. To some this seems to be a positive advantage. Natural selection, they believe, will compel the adoption of the best system. This is a very short sighted view.

It is not the chance to pay taxes that attracts men and business to a place, but the chance to avoid payment. Under a system of home rule the temptation to make concessions, if not to individuals at least to classes, would be very hard to resist. To take but one example: it is by no means improbable that one of our cities, in its desire to secure manufactures, would offer low rates of taxation or complete exemption. This would, perhaps, have a beneficial effect on that city, so long as the others did not follow its example. Competition, when it works smoothly, is beneficial—to those who deal with the competitors, not necessarily to the competitors themselves. When competion works ill it is likely to benefit a few at the expense of the rest.

A little consideration of the economic character of this competition will throw some light on its probable effects. Taxes are justified by the expenses necessary for the conferring of common benefits. It is not possible to make particular payments conform to particular benefits nor to the cost thereof. The coming of a given industrial establishment doubtless increases the cost of government, but this cost cannot be estimated, and its coming brings benefits as well as costs. This establishment may have a very high taxpaying ability, but even from a fiscal point of view—and it is very hard for a community in such a matter to confine itself to the fiscal point of view—it may be better to charge it a low rate than to let it go elsewhere. Even under the existing conditions there is a strong temptation for localities to bid for the presence of objects that can be taxed by giving them a low valuation.

In this respect taxes somewhat resemble railroad rates, but the analogy is not perfect and care must be taken not to push it too far. Where unrestrained competition exists railroads will often carry traffic at any rate that will cover the actual cost of handling and contribute even a trifle to the general expenses, though it might fairly be called upon to pay a large share of them. It is precisely this principle that

has led the railroads to make gross discriminations between places and even between persons, allowing large rebates to powerful shippers.

While there is some doubt as to how far competition between different branches of the government is beneficial, conspicuous illustrations of the reverse effect are not lacking. The intolerable evils of commercial competition between the states were among the chief causes of the adoption of the National Constitution, which, among other provisions relating to commerce, forbids the imposition by the states of customs duties. It was by reason of states' rights that New Jersey and some of the other states were able to provide facilities for the establishment and maintenance of the trusts, notwithstanding the laws of other states and of the National Government against them. It is interesting to note that one of New Jersey's objects seems to have been the desire to secure revenue by the taxation of corporations.

§12. The proposal for a separation of the sources of state and local revenue is commonly discussed in connection with home rule. The two, however, have no necessary connection with each other. They rest, in the main, on entirely different principles, and the former might be adopted without the adoption of the latter. Indeed, a beginning has already been made. The State alone receives the revenue from the inheritance tax, from the taxes on insurance premiums, and from those on the gross receipts of express and private car companies. The poll tax, so far as it exists at all, is a local tax, and the cities make use of a considerable number of business licenses in the revenue from which the State has no share. As regards the chief form of taxation, however, there is no such separation.

Of the arguments in favor of separation two only will here be considered. The first rests on the relation of the particular source of revenue to the government, and the second on practical questions of administration.

There are some sources that, in a way, seem particularly appropriate to the State and others to the localities. As we have already seen a large portion of the property of the inter-county public service corporations, especially that represented by the franchise, is incapable of very definite location, and might reasonably be attributed to the State. Not only is the value difficult to apportion, but it is largely dependent on state functions. The same may be said of the value of corporation franchises generally, not including the special franchises granted by municipalities. On the other hand the value of the tangible property of corporations, while presenting some difficulties, especially

in the case of companies doing an inter-county business, seems to be largely a local matter. If a separation were made real estate would seem to be particularly appropriate to the localities because of the close relation between its value and local functions and expenditures. This applies to such property as railroad terminals as well as to other forms of real estate.

There are clearly some subjects that can be adequately assessed only by the state. Here, again, the public service corporations are conspicuous. On the other hand, if there is anything that is particularly suitable for local assessment it would seem to be real estate. The reason for this is that a knowledge of local conditions is desirable; but assessors with a knowledge of local conditions could, and presumably would, be chosen under state assessment. Our whole study of assessment has pointed to the desirability of at least a large measure of state control. To be sure this is partly due to the difficulties of inter-county equalization, which presumably would be done away with under the separation of the sources, but it is by no means entirely so. As we have seen local assessors are under a very strong temptation to attract taxpayers by a low valuation. Indeed, local control of assessment has some of the chief disadvantages of home rule, with the additional disadvantage that if concessions were made it would be less likely to be done frankly and openly.

It would seem that complete separation of the sources would almost certainly result in serious inequalities. It is highly improbable that sufficient sources of revenue especially appropriate to the state could be found. It would be necessary either to utilize for the state sources especially appropriate to the localities or to abandon the idea of complete separation. The former plan would probably result in considerable inequalities between the localities.

It is sometimes said that the state should rely largely on indirect taxes. As we have already seen, these may legitimately be used as a part of the system, and this is true whether the system be national, state, or local. It is also true that they should not be used exclusively by any of these governmental agencies. Where they are serious inequalities are almost certain to result. Besides this they are generally inelastic. Both the state and the localities need an elastic element in their tax systems. In both cases this should be a direct tax, and should be applied so broadly and with such a degree of equality that no important set of persons would be under the temptation to approve large public expenditures with the idea that the burden would be borne by

someone else. To provide separate and satisfactory taxes of this sort for the state and the localities would be very difficult and there is much ground for the fear that it could not be done.

It does not, of course, follow that there should be no separation. Some taxes are especially suited for state, some for local use. To a limited extent we have this separation now, and it is not improbable that when the tax system is revised we shall have it to a still greater extent. Complete separation, however, is hardly desirable; and it is interesting to note that as between the states and the national government the movement is in the other direction.

§18. Whatever changes are made the existence of a state tax commission is a matter of vital importance. On this point there would be little or no disagreement among the authorities on taxation, and their views are well confirmed by experience in this and other states. Opposition to the present board, which shows itself biennially, seems to be based partly on a misunderstanding of its functions, partly on opposition to what it has done.

As regards the functions of the board a good deal has been said in our discussion of the existing system, and only a brief summary is needed here. Firstly, it has a general oversight of the tax system. Its members are supposed to be authorities on the subject, and so familiar with the actual conditions as to enable them to make suggestions and recommendations to the Governor and the Legislature. In short, it is the State's official adviser on taxation matters. In general its recommendations have been good, and some of them have been adopted with beneficial results. Secondly, it has supervision over the county assessors and is their official adviser and instructor. There can be little doubt that the administration of the state law has been made more effective through its efforts. Taking them as a whole, the assessors seem strongly opposed to the abolition of the Board. Thirdly, it has collected the very important information on which state equalization must rest. While it has probably fallen short of success in this matter, it must be remembered that it has had a well nigh impossible task. Heretofore its members have been members of the State Board of Equalization. Upon the whole there is little reason to doubt that as a result of its work state equalization has been improved. Fourthly, it has had direct responsibility for the assessment of the operating property of railroad and telegraph companies. While it is possible that this work could be done by the Public Service Commission, it must be remembered that taxation and regulation are two distinct things,

and that the valuations suited for the two purposes are frequently different. As we have seen the work of the Board as assessor should be extended rather than reduced. Finally, it has direct charge of the administration of a number of state taxes, including those on the gross earning of express and private car companies, and the very important inheritance tax. In connection with the latter it has had under its care the state's interest in escheats. There are one or two other functions that might be mentioned, but they are not essentially a part of its work as a tax commission.

It is not, of course, contended that the work of the Board has been so good that nothing can be said against it. Doubtless, even under the circumstances, there are respects in which improvement is possible. It must be remembered, however, that the system with the administration of which it is charged has practically no friends among those who are generally regarded as authorities upon the subject. If it has failed to make the system work well it has failed where many have tried, under a great variety of conditions, and none has succeeded. It seems clear, however, that it has made the system much more effective than it would otherwise have been. In the process, no doubt, some evils have been made more effective. Opposition, however, should be aimed at the system which is responsible for the evils, not at the commission whose duty it is to make the system effective.

If a satisfactory system of taxation were established the need of a commission—or possibly even of a tax department—would probably be much greater than it is today. The present system is fairly simple. It is altogether too simple—and too crude—for the difficult and delicate function it is intended to perform. A scientific system will necessarily be somewhat more complex, and it must be scientifically administered. The commission might, perhaps, be reorganized, but the change should be in the direction of increasing rather than of diminishing its importance. There should be some one body having general oversight of the entire system, able to direct its subordinates and able to inform and advise its superiors.

§14. Our system of taxation was adopted when we were a small frontier community. Since then we have become a great commonwealth, a part of a highly complex civilization. Our methods of taxation have not developed in anything like a corresponding manner. It need not be denied that the adoption of methods suited to present conditions will be accompanied by some difficulties, and perhaps some dangers. The latter, however, are hardly likely to be greater than

the dangers of attempting to confine ourselves to a system that we have outgrown. A change of some sort is pretty sure to come. If we proceed to this change with an earnest desire to do justice and to accept the light that science can give, we may expect, not indeed perfection, but a condition in keeping with our place as a great state, and highly favorable to our own prosperity.

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